Congressional
October 1979

Delivered to Sen. Morgan
10/23/79

Paul A. Volcker

Senator -

I thought you would be interested in the attached, which I have sent to Senator Proxmire at his request.

I'm sorry that we didn't seem able to get together on this - but I am sure you understand the nature of my concern.

Best regards,
Paul

CN1
#89

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

PAUL A. VOLCKER
CHAIRMAN

October 23, 1979

The Honorable Adlai E. Stevenson
United States Senate
Washington, D. C. 20510

Dear Senator Stevenson:

Your letter of October 22 requests our views on an amendment to section 5169 of the Revised Statutes contained in section 412 of the "Depository Institutions Deregulation Act of 1979," H. R. 4986, recently reported by the Senate Banking Committee.

Last year, section 5169 of the Revised Statutes was amended by section 1504 of the Federal Institutions Regulatory and Interest Rate Control Act of 1978, to provide that a National Bank Association heretofore or hereafter chartered "is not illegally constituted solely because its operations are or have been required by the Comptroller of the Currency to be limited to those of a trust company and activities related thereto." Section 412 of H. R. 4986 would further amend this section of the Revised Statutes to provide that such a nationally chartered limited purpose trust company "shall be deemed an additional bank within the contemplation of section 3 of the Bank Holding Company Act of 1956."

Section 3(d) of the Bank Holding Company Act of 1956, as amended, provides that a bank holding company may not acquire "any additional bank located outside of the State in which the operations of such bank holding company's banking subsidiaries were principally conducted on the effective date of this amendment. . . ." However, this interstate prohibition would not be applicable to a limited purpose trust company because the Bank Holding Company Act now defines a bank to be an institution that (1) accepts demand deposits, and (2) engages in the business of making commercial loans.

Under the Bank Holding Company Act and Regulation Y issued thereunder, a trust company is considered to be a nonbanking activity and trust company activities are one of the activities determined by the Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

The proposed amendment in section 412 of H. R. 4986 represents an attempt to protect present providers of trust services from prospective competition. In general, the Board has found that both de novo and across State lines entry into authorized nonbanking activities add an extra competitive dimension. Consequently, the limitations proposed in section 412 have anticompetitive implications and, as such, threaten to have an adverse impact on the public interest in the availability of competitive sources of trust services.

Moreover, it should be noted that section 412 introduces a distinction between Federally chartered and State chartered institutions in the Bank Holding Company Act. Under the provisions of this amendment, State chartered limited purpose trust organizations would not be subject to the limitation on banks under section 3(d) of the Bank Holding Company Act, but would continue to be subject to the nonbank provisions of that Act.

I trust that these views will be helpful to you in your consideration of this amendment.

Sincerely,

S/Paul A. Volcker

ADLAI E. STEVENSON
ILLINOIS

United States Senate
WASHINGTON, D.C. 20510

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
SUBCOMMITTEE ON INTERNATIONAL FINANCE (CHAIRMAN)
COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION
SUBCOMMITTEE ON SCIENCE, TECHNOLOGY AND SPACE (CHAIRMAN)
SELECT COMMITTEE ON ETHICS (CHAIRMAN)
SELECT COMMITTEE ON INTELLIGENCE
SUBCOMMITTEE ON THE COLLECTION, PRODUCTION AND QUALITY OF INTELLIGENCE (CHAIRMAN)
DEMOCRATIC POLICY COMMITTEE

October 22, 1979

#84

Mr. Paul A. Volcker, Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

The "Depository Institutions Deregulation Act of 1979," H.R. 4986, which was recently reported by the Senate Banking Committee, contains a provision, Sec. 412, which would result in an amendment to the Bank Holding Company Act. As the Committee did not consider this issue during hearings, I would appreciate having the views of the Board on Sec. 412.

H.R. 4986 might come soon to the floor of the Senate, and thus your earliest attention to this matter would be appreciated.

Sincerely,

Adlai E. Stevenson

October 23, 1979

The Honorable Henry J. Nowak
Chairman
Subcommittee on Access to Equity Capital
and Business Opportunities
Committee on Small Business
House of Representatives
Washington, D.C. 20515

Dear Chairman Nowak:

Thank you for your letter of October 17 inviting the Board to testify before your Subcommittee at hearings to consider the small business impact of recent Federal Reserve monetary policy actions.

Vice Chairman Frederick H. Schultz will be pleased to appear on behalf of the Board on October 30.

Sincerely,

S/Paul A. Volcker

JFB:pjt (#V-84)
bcc: Gov. Schultz
Eleanor Stockwell
Mrs. Mallardi (2)

HENRY J. NOWAK, N.Y.
CHAIRMAN

TOM STEED, OKLA.
PARREN J. MITCHELL, MD.
FREDERICK W. RICHMOND, N.Y.
BERKLEY BEDELL, IOWA
CLAUDE LEACH, LA.

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TOBY ROTH, WIS.
LYLE WILLIAMS, OHIO

DAVID E. FRANASIAK
SUBCOMMITTEE COUNSEL
202-225-7797

HAROLD L. ARONSON, JR.
MINORITY SUBCOMMITTEE COUNSEL
202-225-4341

United States House of Representatives
Committee on Small Business
Subcommittee on Access to Equity Capital
and Business Opportunities
B-363 Rayburn House Office Building
Washington, D.C. 20515

1979 OCT 19 AM 10: 58

October 17, 1979

#84

Honorable Paul A. Volcker, Chairman
Board of Governors
Federal Reserve System
Constitution Avenue between 20th and 21st Sts.
Washington, D. C. 20551

Dear Mr. Chairman:

The Subcommittee has scheduled a hearing on the subject of the Federal Monetary Policy and how it will affect availability of loans to small business, to commence at 9:00 a.m. on October 30 next, in Room 2359 of the Rayburn House Office Building, Washington, D. C.

You are invited to appear before the Subcommittee on that date to offer testimony on this important issue. It would be appreciated if you would provide us with 50 copies of your prepared statement by October 25, 1979.

If any questions should arise in connection with your appearance or testimony, please contact the Subcommittee Counsel.

With best wishes and kind regards,

Sincerely,

Henry J. Nowak

Henry J. Nowak
Chairman

CM
#29

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

PAUL A. VOLCKER
CHAIRMAN

October 22, 1979

The Honorable Jerry M. Patterson
House of Representatives
Washington, D. C. 20515

Dear Mr. Patterson:

Your September 12 letter requests the Board's views on the concerns you have regarding the proposed blanket exemption from the prohibitions of H. R. 2255 for bank holding companies with total assets of $50 million or less and whether expansion by such exempt bank holding companies and their subsidiaries would be subject to the public benefits test of section 4(c)(8) of the Bank Holding Company Act ("Act") raised during the mark-up session on H. R. 2255. The numbered paragraphs below correspond to the specific questions you have asked.

(1) It is the Board's opinion that permitting an activity to be engaged in by a bank holding company or its subsidiary solely because of the asset size of the bank holding company is not relevant to a determination of whether an activity is closely related to banking within the meaning of section 4(c)(8) of the Act. By employing such a standard Congress would be abandoning some well established criteria that have been developed over the years by the courts and have come to be recognized as appropriate for determining whether a nonbanking activity is "closely related" to banking within the meaning of section 4(c)(8) of the Act. (National Courier Association v. Board of Governors, 516 F.2d 1229, 1237 (D.C. Cir. 1975), and Alabama Association of Independent Insurance Agents v. Board of Governors, 533 F.2d 224, 241 (5th Cir. 1976).) Furthermore, an institution's size alone is not a determinant of the potential for abuse, but should be considered in the context of the market in which the institution operates. For example, a bank holding company of less than $10 million in assets might be the only financial institution in a town and its ability to exert an unfair competitive influence would be much greater than a $200 million institution located in a major metropolitan market.

(2) The $50 million exemption would permit such an organization to engage in insurance activities otherwise not permissible to a bank holding company with greater assets. Under such an exemption, insurance

activities that could be engaged in would include the sale of property and casualty insurance and underwriting of such insurance. The Board's regulation, however, does not permit the underwriting of property and casualty insurance. Thus, there would be a broadening of the permissible product line of insurance for smaller companies beyond those currently permitted by the Board's regulation governing insurance activities of bank holding companies.

(3) The $3500 finance company transaction exemption could have the effect, for example, of restricting finance companies as an alternative source of credit to borrowers seeking financing for new or used car purchases, unless the lender is willing to forego the insurance or directs the borrower to another source of insurance. It would certainly put a finance company subsidiary of a bank holding company at a competitive disadvantage since other finance companies and lenders are not similarly restricted.

(4) For the same reasons as stated in paragraph three above, the Board does not believe it would be useful or appropriate to base the permissibility of insurance activities on some arbitrary loan amount.

(5) Enclosed for your consideration is the Appendix to Governor Partee's testimony of October 17, 1979, before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance that sets forth in some further detail the Board's views and its comments on the insurance provisions of H. R. 2255, H. R. 2747 and H. R. 2856, as well as other provisions of those bills.

Finally, your letter indicates concern that the public benefits test in section 4(c)(8) of the Act might not be applicable to insurance activities engaged in by bank holding companies of less than $50 million in total assets. Based on the legislative history the Board believes that section 4(c)(8) imposes a two-step test. Court decisions have confirmed that view. A proposed activity first must be determined by the Board to be closely related to banking. If such a determination is made, the activity may be engaged in, or the nonbanking company engaged in the activity may be acquired, only if the Board finds that the public benefits test of section 4(c)(8) is met. That is, the Board must find that the likely benefits to the public that would result from a bank holding company engaging in the activity outweigh possible adverse effects that may result therefrom. Thus, if the legislation as proposed is enacted, the closely related criteria would be statutorily determined, but whether a

The Honorable Jerry M. Patterson
Page Three

specific proposal would meet the public benefits test of section 4(c)(8) would remain to be determined by the Board in connection with individual proposals.

Thank you for this opportunity to offer our views on these matters and please do not hesitate to contact us further.

Sincerely,

S/Paul A. Volcker

Enclosure

October 22, 1979

The Honorable Fernand J. St Germain
Chairman
Subcommittee on Financial Institutions
Supervision, Regulation and Insurance
Committee on Banking, Finance and
Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Chairman St Germain:

Thank you for your letter of September 14, 1979, requesting our opinion on the impact of H.R. 2255, as amended, on relevant State law. We understand that in particular you request comment on the $3,500 limitation of section 1(B) and section 2 of the bill.

The Board's Legal Division has considered the provisions of H.R. 2255 in the context of the questions posed during the Subcommittee markup. It is the opinion of the Legal Division that the $3,500 limitation of section 1(B) of the bill applies only to the amount of insurance that a bank holding company may provide pursuant to Federal law as principal, agent or broker in connection with an extension of credit by a finance company subsidiary of the bank holding company. Under section 7 of the Bank Holding Company Act, 12 U.S.C. § 1846, the amount and kinds of insurance that a bank holding company may provide may be further restricted but not expanded by State law. However, were section 2 of the amended bill enacted, a State could enact legislation that might expand the amount and kinds of insurance a bank holding company may provide.

The restrictions of section 1(B) apply only to the insurance provided in connection with an extension of credit by a finance company subsidiary of a bank holding company and are distinct from any restrictions on the lending authority of such a subsidiary, which restrictions to date have been imposed only by State and not Federal law. Therefore, the restrictions of section 1(B) would have no impact upon the lending authority of finance company subsidiaries of bank holding companies, and would impact the lending activities of such subsidiaries only insofar as customers of finance companies legally lending in excess of $3,500 may prefer to do business with companies able to make the loan and sell related insurance, that is, companies not affiliated with a bank holding company.

Section 2 of the bill provides that the amendment made by section 1 shall not supersede existing State laws and shall not be effective in any State when such State enacts a law contravening the amendment made by section 1 of the bill. The Board's Legal Division believes that, for the reasons discussed above, section 2 is unnecessary to meet the concerns of Subcommittee members relating to restrictions on lending authority. Further, we note that the effect of section 2 would be to enable States to act to permit insurance activities that would be prohibited by section 1. We believe, however, that even in those instances in which State authorities enact legislation finding certain insurance activities "closely related" to banking, the Board would still be required to find those proposed activities "closely related" to banking and to apply the public benefits test under section 4(c)(8) of the Act. In this regard, the Board in the past has found certain of the activities prohibited by section 1 to meet these two criteria.

If you have any further questions regarding these matters, please do not hesitate to contact us.

Sincerely,

S/Paul A. Volcker

RW:MEB:RM:DJW:pjt (#V-32)
bcc: Rich Whiting
Mike Bleier
Bob Mannion
Mrs. Mallardi (2)

CM
#25

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

PAUL A. VOLCKER
CHAIRMAN

October 22, 1979

The Honorable Parren J. Mitchell
Chairman
Subcommittee on Domestic Monetary Policy
Committee on Banking, Finance and
Urban Affairs
House of Representatives
Washington, D. C. 20515

Dear Chairman Mitchell:

I want to thank you for the support of our recent policy initiatives expressed in your letter published by the Wall Street Journal on October 11. I find such support most encouraging and helpful as my colleagues and I seek to assure that monetary policy will do all that it can to help bring inflation under control.

I have also given careful thought to the points made in the earlier letter that you and members of your Subcommittee sent me concerning long-term monetary objectives and their relation to the economic objectives contained in the Humphrey-Hawkins Act. As I see it, the thrust of your earlier remarks is directed at two major points: first, that the rate of monetary growth should gradually but systematically be reduced to the perceived non-inflationary rate of 3 percent by 1982; and, second, that the Federal Reserve should commit itself to an explicit long-range target path of monetary growth along the lines set forth in your letter.

I agree fully with the philosophy underlying your remarks. My Federal Reserve colleagues and I are strongly committed to a policy of establishing and maintaining a non-inflationary rate of monetary expansion and we seek to achieve that goal in the most orderly and expeditious fashion. In this fundamental sense, we share a common viewpoint.

On reflection, I don't think we are far apart on the approach to meeting this objective. But I am uneasy about establishing precise monetary targets over a multi-year time frame. In my view the Federal Reserve needs the flexibility to respond to situations as they arise--including the admittedly remote possibility that shifting expectations might permit a more prompt move in the direction that we both see as appropriate. However, you should not associate my reluctance to subscribe to specific long-term quantitative targets as being indicative of any doubt as to the merits of the underlying policy objective. Our recent policy actions serve to underscore the System's determination to achieve a non-inflationary rate of monetary growth.

In seeking to meet our objective, your continued support will be helpful and appreciated.

Sincerely,

S/Paul A. Volcker

Assigned to Mr. Axilrod

PARREN J. MITCHELL, MD., CHAIRMAN

STEPHEN L. NEAL, N.C.
NORMAN E. D'AMOURS, N.H.
DOUG BARNARD, GA.
JIM MATTOX, TEX.
JOHN J. CAVANAUGH, NEBR.

225-7315

U.S. HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON DOMESTIC MONETARY POLICY
OF THE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SIXTH CONGRESS
WASHINGTON, D.C. 20515

#25

September 5, 1979

The Honorable Paul Volcker
Chairman, Board of Governors of the
Federal Reserve System
Federal Reserve Building
Washington, D.C. 20551

Dear Mr. Volcker:

We appreciate having received courtesy copies of the letter you sent on August 16, 1979 to the Honorable Henry S. Reuss, Chairman of the House Banking Committee. It is a pleasure and reassurance to know, at the outset of your tenure at the Board of Governors, that you take the monetary policy report of this Committee seriously, and that you approach the report process as a constructive dialogue.

In the spirit of that dialogue, we want to point out to you that at least one major recommendation in the Committee's monetary report still has not been dealt with by the Federal Reserve, even in your letter. That recommendation is that the Federal Reserve should set longer-term goals, so that we can see clearly the path that will be followed in attaining the overall economic goals of the Humphrey-Hawkins Act.

Specifically, the last paragraph of the Committee's report of July 27, 1979, said the following:

> "Your committee agrees with the Federal Reserve that its previously established growth ranges for the monetary aggregates for 1979 are still appropriate. We are, however, disappointed that the Federal Reserve has failed to set longer-term targets for progressive deceleration in monetary growth, such as we recommended in our report of March 12, 1979. Because, as your committee stated in that earlier report, achievement of the interim 1983 goals of the Humphrey-Hawkins Act (4 percent unemployment and 3 percent inflation) would be promoted by steady deceleration in the average annual rate of monetary expansion over the next 5 years, we renew our recommendation for the establishment of the long-term targets we specified in the report of March 12, 1979, as follows:

Recommended percent growth 4th quarter to 4th quarter M1 (adjusted) 1978-83

	Percent
1978	7.6
1979	6.0
1980	5.0
1981	4.0
1982	3.0
1983	3.0

We note that the Federal Reserve's "tentative" ranges for 1980 growth in M1 (adjusted for ATS accounts) would "permit" attainment of our recommended rate of growth for that year, but it is disquieting that the Federal Reserve has set its range for M1 (adjusted) such that the mid-point is well above our recommendation. We would be much happier if the Open Market Committee would set its short-term targets with an explicit connection to a longer-term target path which promises achievement of the Humphrey-Hawkins goals. If you and your colleagues believe that the Committee's recommended 1979-1983 monetary growth path is wrong, certainly it should be explained why you do and an alternative proposed.

Without an explicit longer-term monetary growth target path, and an explicit and defensible connection of the shorter-term targets to that path, we find it difficult to accept the Federal Reserve's position that it is, in its short-term operations, advancing toward the achievement of the 4% unemployment and 3% inflation goals for 1983 specified by the Humphrey-Hawkins Act. We trust that the Board will not again, in its next regular report, pass over this subject in silence. More importantly, we hope that the Federal Reserve will be able to report to us early in 1980 that it has conducted monetary policy in a way that shows clear progress in attaining the goals of Humphrey-Hawkins, whatever the short-term temptations may be to focus on illusory short run interest rate targets.

Sincerely,

Steve Neal

Parren J. Mitchell

Doug Barnard Jr

Jim Mattox

Norm D'Amours

October 18, 1979

The Honorable Elwood H. "Bud" Hillis
House of Representatives
Washington, D.C. 20515

Dear Mr. Hillis:

Thank you for your letter of October 16 which contains the constructive suggestion that I consider meeting regularly with House members in a closed door situation to discuss current economic issues and policies.

I do welcome the opportunity to meet informally with House members to discuss the economy and in recent weeks have met with the 95th Caucus and the SOS-Chowder and Marching Society.

I would be happy to meet with any group you wish to put together.

Sincerely,

S/Paul A. Volcker

KAG:pjt (#V-80)
bcc: Mrs. Mallardi (2)

ELWOOD H. "BUD" HILLIS
5TH DISTRICT, INDIANA

COMMITTEES:
HOUSE COMMITTEE ON VETERANS' AFFAIRS
HOUSE ARMED SERVICES COMMITTEE
CHAIRMAN:
REPUBLICAN TASK FORCE ON ENERGY AND ENVIRONMENT

#8

Congress of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
2429 RAYBURN BUILDING
TELEPHONE: 202-225-5037

KOKOMO OFFICE:
518 NORTH MAIN STREET
TELEPHONE: 457-4411

ANDERSON OFFICE:
26 WEST 7TH STREET
TELEPHONE: 642-8023

MARION OFFICE:
220 MARION P.O. BUILDING
TELEPHONE: 662-7227

October 16, 1979

1979 OCT 17 PM 12:21

The Honorable Paul A. Volcker
Chairman
Board of Governors of the
Federal Reserve System
Twentieth Street and Constitution, N.W.
Washington, D.C. 20551

Dear Chairman Volcker:

More than any other single issue, inflation touches the lives of every American. I am constantly asked by constituents to comment on the economy. Many times my constituents are looking for reassurance that a major recession is not forthcoming and that inflation will soon subside. On other occasions, people just want to know why the economy is in its present state.

Like all elected officials, I consider it a major part of my job to help educate my constituents so that they may better understand issues. However, since I do not serve on a Congressional committee which directly oversees or has responsibility for economic policies, it is difficult to understand all the complexities involved with economic matters.

As the Chairman of the Federal Reserve, you are in a unique position to assist in the tutelage of Members of Congress such as myself. Unfortunately, there is seldom an opportunity for you to discuss candidly the policies of the Federal Reserve with most Members. Therefore, I would like to make a suggestion that I believe would prove beneficial to all concerned.

If you or your designate would come to Capitol Hill on a regular basis to meet with Members only in a closed door situation to discuss current economic issues and policies, I believe you, the Members and their constituents, would all profit. Similar meetings are often held by the State Department for the purpose of discussing international issues. I have found these meetings to be of value. While I realize that your schedule is already full, I am convinced that holding such meetings would be time well spent.

Sincerely,

Bud Hillis

Elwood H. "Bud" Hillis
Member of Congress

H:s:v

October 18, 1979

The Honorable Alan Cranston
United States Senate
Washington, D.C.   20510

Dear Alan:

Thank you for your recent letter recommending Ms. Nancy Spillman as a member of the Board's Consumer Advisory Council.

I can assure you that Ms. Spillman's qualifications will receive full consideration by the Board when it makes the 1980 appointments to the Council within the next several weeks. We will be in touch with you when the selections are made.

The Board appreciates receiving your recommendation and your interest in the Consumer Advisory Council.

Sincerely,

S/ Paul

CO:pjt (#V-61)
bcc: Mrs. Mallardi (2)

ALAN CRANSTON
CALIFORNIA

United States Senate
WASHINGTON, D.C. 20510

October 5, 1979

#61

1979 OCT -9 PM 4:32

Honorable Paul Volker
Federal Reserve System
Board of Governors
Washington, D.C. 20551

Dear Paul,

It's a pleasure to recommend a friend and fellow Californian, Nancy Spillman, to serve on the Federal Reserve Board's Consumer Advisory Council.

Nancy's background in consumer economics needs little introduction -- she is among the better-known and respected teachers, writers and lecturers in the field. Active in a number of consumer-oriented groups, she has given tremendous dedication and energy to the cause of educating the American public on consumer affairs.

In my opinion, few professionals in consumerism and economics have offered as much of themselves in the effort.

I believe Nancy Spillman could make a significant contribution to the work of the Consumer Advisory Council, and urge you give her qualifications your most serious consideration and review. Enclosed are additional background materials pertinent in this regard.

Best wishes,

Sincerely,

Alan

Alan Cranston

Enclosures

Enjoyed seeing you the other day, Paul.

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Citation Information

Document Type: Magazine article

Number of Pages Removed: 7

Citations: Spillman, Nancy Z. "Bright Ideas for Consumer Educators." *Previews*, September 1979.

August 13, 1979

Ms. Anne Geary
Assistant Director
Division of Consumer Affairs
Board of Governors of the Federal Reserve
Washington, D.C. 20551

Dear Ms. Geary:

Ms. Nancy Spillman, Editor of our Consumer Education Forum has indicated to me that she has been nominated to serve on the Federal Reserve Board's Consumer Advisory Council. I support this nomination without reservation.

In addition to her service to the American Council on Consumer Interests, Ms. Spillman has:

(1) Authored a text, Consumers: A Personal Planning Reader

(2) Reviewed a substantial quantity of consumer education resources

(3) Been a member of the California State Attorney General's Subcommittee on Consumer Education

(4) Been author of a monthly column, "Consumer Corner" for the Braille Mirror.

I have worked with Ms. Spillman since she became Editor of our Forum. I have found her to be a competent, conscientious, and committed professional. If her nomination to the Advisory Council is accepted, I am certain that the Board will be delighted with her professional involvement.

Sincerely yours,

Mel J. Zelenak
Executive Director

MJZ/csh

NFIB National Federation of Independent Business

August 15, 1979

Ms. Anne Geary, Assistant Director
Division of Consumer Affairs
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Ms. Geary:

On behalf of the National Federation of Independent Business, I wish to support Arthur H. Bronson's nomination of Miss Nancy Z. Spillman for a position on the Federal Reserve Board's Consumer Advisory Council. She has worked closely with NFIB's Education Department this year and we are impressed with her overwhelming dedication and varied experience in the fields of economics and consumerism.

Miss Spillman's numerous achievements include serving as the editor of the national newsletter CONSUMER EDUCATION FORUM, the author of a monthly article of consumer tips for the BRAILLE MIRROR, a member of the California State Attorney General's Subcommittee on Consumer Education and a member of the Los Angeles Consumer Credit Counselors. These responsibilities and additional experiences as a speaker, author and educator about consumer affairs, convince me that Nancy Spillman would undoubtedly make a significant contribution to the Federal Reserve Board's Consumer Advisory Council.

Sincerely,

Wilson S. Johnson
President

WSJ/bab

Home Office. 150 West 20th Avenue, San Mateo, California 94403 Telephone (415) 341-7441 / Legislative Office: Washington, D.C

California Loan and Finance Association

11950 SAN VICENTE BOULEVARD, SUITE 213 • LOS ANGELES, CA. 90049 • (213) 820-2478

August 10, 1979

Ms. Anne Geary
Assistant Director
Division of Consumer Affairs
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Ms. Geary:

Nancy Spillman, Director of the Center for Economic Education and Associate Professor of Economics, informed us that she is interested in serving on the Federal Reserve Board's Consumer Advisory Council.

Miss Spillman has been an advocate of the Consumer Credit Industry for years and has been instrumental in the use and distribution of credit educational material from the National Consumer Finance Association. We have read many of her articles and think they are outstanding.

We are honored in recommending her for the Council.

Sincerely,

C. A. Mann
Executive Vice President

October 18, 1979

Dear Mac:

Thanks for your note. Actually I think I better stop talking for a while -- but I do hope what we are doing and what we are saying will help to put a dent in inflationary expectation.

Sincerely,

The Honorable Charles McC. Mathias, Jr.
United States Senate
Washington, D. C. 20510

EGC:slw

CHARLES McC. MATHIAS, JR.

10 October 79

Dear Paul,

Keep on talking!

Not only what you are saying, but the way you are saying it will have an impact on national confidence. The fine impression you made on MacNeil-Lehrer is a case in point.

As ever,

Mac

BILL GRADISON
1st District, Ohio

RON ROBERTS
Administrative Assistant

Congress of the United States
House of Representatives
Washington, D.C. 20515

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Cincinnati, Ohio 45202
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October 17, 1979

The Honorable Paul A. Volcker
Chairman
Federal Reserve Board
20th and C Streets, N.W.
Washington, D.C. 20551

Dear Paul:

Just a note to thank you and Ken for taking time from your busy schedules to visit with our SOS and C & M breakfast group this morning.

It was one of the best meetings we've had, and I hope you enjoyed the give-and-take as much as we did.

Best wishes.

Sincerely,

Bill

Bill Gradison
Representative in Congress
First District of Ohio

BG/t

October 18, 1979

The Honorable Henry S. Reuss
Chairman
Committee on Banking, Finance
and Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Chairman Reuss:

I am not only sympathetic with the views you expressed in your letter of October 12 on the subject of lagged reserve accounting, but have asked that planning go forward on the matter. Concurrent reserve requirements would be more consistent with the System's new approach to monetary policy operations that places more weight on reserves. At the same time, I am not convinced that the existing two week lag between deposits and required reserves is an important complication in achieving reserve and monetary targets over a period of three to six months or so.

In all the circumstances, the Board has preferred to maintain lagged reserve accounting at least for the immediate future in the hope the membership problem can soon be resolved. There is little doubt that such a change will be resisted by many small- and medium-sized banks for, from their standpoint, legitimate reasons.

In any event, we will complete our planning and studies so that we will be prepared to act promptly should the Board feel that present operating procedures reveal a more compelling and urgent need than we now assume.

Sincerely,

S/ Paul

ECE:SHA:PAV:pjt (#V-49 & #V-76)
bcc: Mr. Ettin
Mr. Axilrod
Mrs. Mallardi (2)

HENRY S. REUSS, WIS., CHAIRMAN
THOMAS L. ASHLEY, OHIO
WILLIAM S. MOORHEAD, PA.
FERNAND J. ST GERMAIN, R.I.
HENRY B. GONZALEZ, TEX.
JOSEPH G. MINISH, N.J.
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225-4247

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October 12, 1979 #76

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Volcker:

I believe it is essential for the operation of monetary policy that the Federal Reserve adopt procedures which would facilitate your new policy of directly controlling the monetary aggregates. Therefore, I recommend a return to the system of synchronous reserve requirements which the Federal Reserve used prior to September 1968.

I have suggested this change over the last three years, in the enclosed letters dated May 10, 1977, July 12, 1977, July 21, 1977, November 7, 1977, April 18, 1978, June 21, 1978, August 10, 1978 and September 26, 1979. In addition I asked a distinguished panel of experts to give their views on lagged reserve requirements. As the enclosed material indicates they unanimously urged an end to lagged reserve requirements in order to facilitate monetary policy. The list of economists noted in this correspondence who oppose the use of lagged reserve requirements include present and former members of the Federal Reserve's own staff.

Last year in testimony before this Committee on July 28, Chairman Miller said "in terms of operation it would be preferable to be on a current basis". However he added the caveat that such a desirable change must wait the alleviation of the Federal Reserve's membership problems. Because lagged reserve requirements result in higher than necessary interest rates, it would seem that our priorities would warrant an immediate return to a system of synchronous reserve requirements.

Sincerely,

Henry S. Reuss
Chairman

Enclosures

May 10, 1977

Honorable Arthur F. Burns
Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

Dear Chairman Burns:

I am concerned about the recent jump in the federal funds rate by 55 basis points from the week ending April 6 to the week ending May 4. I would like to know why the federal funds interest rate target has apparently been raised to something like 5¼ percent. Is this part of an effort to offset the bubble in the money supply (M1) which grew by 22.1 percent in April over March.

Would we not be better off with synchronous reserve requirements so that when the Federal Reserve chooses to offset previous increases in the money supply, required reserves would not be stuck at a previously determined high level? Would not a return to synchronous reserve requirements allow the Federal Reserve to follow a steadier course for its federal funds interest rate target?

I appreciate any light you can shed on these issues.

Sincerely,

Henry S. Reuss
Chairman

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

June 24, 1977

The Honorable Henry S. Reuss
Chairman
Committee on Banking, Finance
and Urban Affairs
House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

I am pleased to respond to your letter of May 10 and to your related statement in the Congressional Record of May 26.

In your letter you expressed concern about the increase in the Federal funds rate through the week ending May 4 and asked why the funds rate target had apparently been raised. Your surmise -- that the rise was related to the April upsurge in M-1 -- is essentially correct.

You also asked in your letter whether it was not the case that a return to synchronous reserve accounting would allow the Federal Reserve to follow a steadier course for its funds rate target. In your Congressional Record statement you expressed the view that much of the sharp April increase in M-1 could have been avoided if the Federal Reserve had been using the pre-1968 technique of calculating required reserves synchronously instead of on a lagged basis. You added that "some additional percentage points of unnecessary M-1 growth could have been avoided if the Fed had simply been a little more conservative in the reserves it was creating through open market policy; only a marginal increase in the Federal funds rate would have been necessary to achieve this."

These statements seem to suggest that a return to synchronous reserve accounting would greatly reduce the short-run variability of both the money supply and the Federal funds rate. I do not believe this is so. The considerations involved are technical and rather complex, and I have asked my staff to set them down. Their memorandum, which also discusses the developments of April and early May, is enclosed.

I appreciate the opportunity to provide this information on the important questions you have raised. Please let me know if I can give you further information regarding them.

Sincerely yours,

Arthur F. Burns

Enclosure

TO: Chairman Burns

DATE: June 24, 1977

FROM: Staff

SUBJECT: Questions raised by Chairman Reuss

In a letter to you dated May 10, 1977, and in a statement in the Congressional Record for May 26, Chairman Reuss comments on fluctuations in the Federal funds rate and M-1 during April and early May and suggests that substantial reductions in the short-run variability of both the money supply and the Federal funds rate could be achieved by a return to synchronous reserve accounting from the present system of lagged reserve accounting. This memorandum first addresses the question of the implications of lagged reserve accounting for short-run variability in the money supply and the funds rate. It then briefly reviews the developments of April and early May.

Implications of lagged accounting

Under the present system of lagged reserve accounting, reserve requirements in the current week are based on the deposits outstanding two weeks earlier. Accordingly, open market operations in the current week cannot affect required reserves in the current week. However, open market operations can affect the volume of nonborrowed reserves in the current week. By increasing nonborrowed reserves through open market purchases, the Manager of the System Account can increase the availability of free reserves to banks, which in turn would expand the supply of Federal funds and tend to lower the rate at which

Federal funds are traded. Conversely, open market sales would tend to reduce both nonborrowed and free reserves, decrease the supply of Federal funds, and increase the funds rate. Hence, the Manager can limit variations in the funds rate reasonably closely by undertaking open market operations designed to counter developments that would otherwise influence it.

Under current operating procedures, the FOMC's instructions to the Manager typically specify ranges for 2-month growth rates for M-1 and M-2--ranges that the Committee believes to be consistent with its longer-run monetary growth objectives and ultimately its more fundamental economic goals--and a constraint on inter-meeting changes in the Federal funds rate. The Committee's directive usually calls (1) for maintaining the funds rate near some particular level so long as the 2-month growth rates for the aggregates appear to be near those expected, and (2) for adjusting the funds rate within the specified range if the 2-month growth rates appear to be deviating significantly from expectations. In carrying out the directive, the Manager obviously must pay close attention to the implications of incoming data on the aggregates for likely monetary growth rates over the 2-month period.

One objective of this procedure is to insulate the monetary aggregates to the extent feasible from the effects of supply-related disturbances. These include movements in noncontrolled factors affecting nonborrowed reserves--such as float or Treasury deposits at the

This cost however is an important one because it means the Fed has an increased tendency to accommodate bank led credit expansion under LRA. A deposit created by a bank loan two weeks ago becomes validated M1-money if the Fed accommodates its creation by maintaining stable money market rates in the face of increased loan demand. If this is an effect of LRA, we would expect increased variability in the monetary aggregates which brings us to conclusion (3) in the report.

According to (3) the variability of M1 and M2 growth rates "was not affected by the introduction of lagged reserve accounting." Rather than disputing the analysis of the numbers presented in the staff report we offer, as prima facie evidence against this assertion, the following quote from the November 1971 Federal Reserve Bulletin, p. 880:

> Even when the revised data are examined, there is compelling evidence to suggest a marked increase in the variance of money supply and reserve innovations which coincided with the adoption of the amendment to Regulation D. (See Feige & McGree J.M.C.B. November 1977, p. 548).

With respect to the issue of the effects of LRA on the variability of the Federal funds rate, our own research revealed a standard deviation of weekly fund rate changes of .34 percentage points for the period 1961-1967 compared to .33 for the 1969-1975 period. We concluded that the effects of LRA on funds rate volativity has not been substantial when weekly changes are considered on a relative basis. While mean absolute changes have increased, variations around the mean are about the same for the pre- and post- LRA periods.

The Board's staff final three conclusions, (4) - (6), bear on the compatibility of LRA with current operating procedures (i.e. setting a funds rate through open market operations which is believed to be consistent with the desired monetary aggregate growth pattern). The conclusions reached are that 1) <u>given</u> current operating procedures it is a matter of indifference whether we have contemporaneous or lagged reserve accounting and 2) if a new operating procedure were adopted where reserves rather than the funds rate were controlled on a day to day basis, then lagged reserve accounting would be inferior to contemporaneous requirements because it would undermine the money-reserve relationship. This latter assertion is supported by the evidence presented on pp. 20-23 of the report which shows a deterioration in the money-reserve relationship after LRA was imposed. This is consistent with our finding in the JMCB article (Nov. 1977) which found the contemporaneous money-reserve relation disappears after the amendments to Regulation D were instituted.

Thus conclusion (6) minimizes the possible benefits to switching to a reserve operating procedure and contemporaneous reserve requirements. In addition a primary argument presented against such a policy is the increase

Reserve Banks--and changes in the amount of free reserves that banks wish to hold. If open market operations have the effect of stabilizing the Federal funds rate, they will at the same time substantially moderate--although not necessarily eliminate--the effects of supply-related disturbances on the monetary aggregates.

A second objective is to respond to sustained <u>demand</u>-related disturbances in a manner that will set in motion corrective forces--i.e., forces tending to move growth of the aggregates back toward their expected path. When, for example, incoming data for the aggregates suggest that the 2-month growth rates are likely to be unduly high relative to the Committee's expectations, the Manager will attempt to induce whatever increase in the funds rate is consistent with the Committee's instructions by an appropriate reduction in the rate of growth of non-borrowed reserves. Other things equal, the increase in the cost of Federal funds would give banks an incentive to rely more on other sources of funds, such as sales of Treasury bills, and to become more conservative in their lending policies. As a consequence of such actions by banks, bank customers and other participants in financial markets are given incentives to economize more on their holdings of money. Such reactions would tend to slow the growth in the aggregates.

Given these procedures and objectives, the choice between lagged and synchronous reserve accounting is of relatively little significance. Whichever accounting system is used, the incoming data on the monetary aggregates--on which operating discussions are based--would be available on the same timing; the Manager could attain his objectives for the funds rate with about the same precision and speed; and the portfolio reactions of banks and others to a change in the funds rate would be much the same. Accordingly, under current procedures a return to synchronous accounting would not reduce the short-run variability of either the monetary aggregates or the funds rate. With respect to the former, the average variability of monthly M-1 growth around trend was about the same in the six years after lagged reserve accounting was introduced as in the preceding six years. The average variability has been somewhat higher in the two most recent years, but this could hardly be attributed to lagged accounting.

Developments in April and early May

Under current procedures, open market operations undertaken to damp demand-related fluctuations in the rates of growth of the monetary aggregates produce fluctuations in the Federal funds rate. More generally, efforts to reduce the variability of either monetary growth rates or of the Federal funds rate can be expected to produce increased variability in the other.

As indicated above, in his day-to-day operations the Manager takes account of fluctuations in the incoming data on the aggregates. Many of these fluctuations are transitory--they are "noise" rather than indications of a systematic departure from desired monetary growth rates. It is usually--although not invariably--difficult to distinguish between noise and systematic tendencies in the data. At the same time, there are costs in mistaking one for the other. To react to what eventually proves to have been only noise is to produce unnecessary, and therefore undesirable, fluctuations in money market rates. To delay reacting to what eventually proves to have been the beginning of a systematic tendency is to necessitate an ultimate reaction that is larger and more abrupt than otherwise would have been necessary.

In order to reduce the risks of mistakes in either direction, current operating procedures call for the Manager to follow a middle course in carrying out the Committee's instructions. He scales any changes in objectives for the funds rate to the apparent strength of the evidence that some systematic departure from desired monetary growth rates is under way, and he stands ready to reverse course if necessary. Among the factors he takes into account are the magnitude of the movements in the monetary data, their duration, and the indications, if any, that they might partly or wholly reflect special factors of a nonpersistent kind.

The developments of April and early May are a case in point. Data that became available immediately after the April FOMC meeting suggested that the money supply was growing rapidly in April. However, because there was some reason to think this pattern would not persist, operating objectives were not modified significantly. By late April, evidence had begun to accumulate that the money supply was growing strongly relative to the Committee's expectations. Accordingly, the Manager raised the objective for the funds rate gradually, to the upper limit of the range the Committee had specified. On May 6 the Committee members voted to increase the upper limit somewhat, on the understanding that the additional leeway would be used only if new data becoming available before the May meeting suggested that the aggregates were strengthening significantly further. Because such additional strength did not develop in that period, the objective was not raised further.

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

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WASHINGTON, D.C. 20515

July 12, 1977

Dr. Arthur F. Burns
Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

Dear Dr. Burns:

Thank you for your reply and accompanying staff report of June 21, to my letter of May 10 questioning the desirability of lagged vs. synchronous reserve requirements. I do not believe that the staff report supports your position in favor of lagged reserve requirements or adequately addresses the issues.

Stated simply, the question is whether a return to synchronous reserve accounting would make it easier for the Fed to manage the money supply and interest rates so that we could, to a large extent, avoid wild short-run fluctuations in the money supply and interest rates such as occurred during April and May of this year. I am sure you would agree that the roller coaster behavior of the money supply during April and May was not a desirable episode for instilling confidence in the monetary management of our economy nor was the sudden rise in the interest rates during May anything but a signal to reduce spending and investment. If the use of lagged reserve accounting helped to accentuate this episode more than would have been necessary with synchronous requirements, then it is high time to switch to synchronous accounting.

Your staff report bypasses the extensive literature and empirical tests produced inside and outside the Federal Reserve by experts who say again and again that lagged reserve accounting interferes with proper monetary management. Here are some examples of views of reputable experts in this field which are not addressed in your staff report.

George G. Kaufman who is now John P. Rogers, Professor of Banking and Finance at the University of Oregon and author of the widely used book Money, the Financial System and Economic Activity, formerly the Assistant Vice President and Economist at the Chicago Federal Reserve Bank, circulated a memorandum on June 13, 1966, within the Federal Reserve System on the proposed change to lagged reserve requirements (Memorandum Federal Reserve Bank of Chicago, June 13, 1966, Subject: Report of Ad Hoc Subcommittee on Reserve Proposals) in which he declared "the lagged reserve scheme would result in a serious deterioration of monetary control by the Federal Reserve". In his letter to me of June 9, 1977, Professor Kaufman says "the evidence to date has not caused me to change my analysis or conclusions".

Albert E. Burger, Assistant Vice President of the Federal Reserve Bank of St. Louis, has this to say about lagged reserve requirements in his 1971 book, The Money Supply Process: "In the sample period following the introduction of lagged reserve requirements there was considerably greater variability in the excess reserve ratio, which introduced an additional element of variability into the money supply process" (page 54). In addition, Burger states "the evidence indicates that after lagging, the Federal Reserve has been less able to accurately determine the extent to which it should intervene in the money market to prevent short-term pressures" (page 56).

Warren L. Coats, Jr., an economist at the International Monetary Fund, published an article "Regulation D and the Vault Cash Gain" in the June, 1973, issue of the Journal of Finance (pages 601-607). Dr. Coats alleges from his study at the Federal Reserve Bank of Chicago that under the lagged reserve rules used by the Fed, banks are allowed to shift reserves between vault cash and deposits at the Fed in such a way as "to weaken the Federal Reserve's control over reserves, hence over the money mechanism" (page 601). Coats's doctoral dissertation at the University of Chicago, "The September, 1968, Changes in Regulation D and their Implications for Monetary Control" (June, 1972) presents a case against lagged reserve requirements.

R. Alton Gilbert, an economist at the Federal Reserve Bank of St. Louis, published an article in the September-October, 1973, Financial Analyst Journal ("The Effects of Lagged Reserve Requirements on the Reserve Adjustment Pressure on Banks") in which he states: "The example of bank reserve management developed in this article indicates that lagged reserve requirements tend to increase variability of reserve adjustment pressure on the individual bank -- the opposite of the intended result." Gilbert goes on to say that "evidence from studies on monetary control under lagged reserve requirements also indicates that the variability of aggregate reserve adjustment pressure has been larger under lagged reserve requirements than under coincident reserve requirements. Thus, there is reason to believe that the regime of lagged reserve requirements has failed in both its objectives "to make management of reserves easier for commercial banks" and make monetary management by the Fed more efficient (page 42). Gilbert cites other studies which criticize lagged reserve requirements including one by Dr. Robert D. Laurent, an economist at the Federal Reserve Bank of Chicago, whose unpublished paper is called "Lagged Reserve Requirements -- Are They Lagged in the Wrong Direction?"

William Poole, Professor of Economics at Brown University and formerly senior economist at the Board of Governors and Assistant Vice President at the Boston Federal Reserve Bank, and Charles Lieberman, Assistant Professor of Economics at the University of Maryland, have published in the Brookings Papers on Economic Activity an article attacking lagged reserve requirements ("Improving Monetary Control", 1972, pages 293-317). They conclude, "In any event, the lagged requirements system does not make reserve management any easier for the banks and does tend to intensify money market instability" (page 312).

Nowhere am I able to find an economist who has investigated reserve requirements who would say that control of the aggregates is easier under lagged than synchronous reserve requirements. The following statement in your staff study in no way contradicts this position. "If open market operations have the effect of stabilizing the Federal funds rate, they will at the same time substantially moderate -- although not necessarily eliminate -- the effects of supply related distrubances on the monetary aggregates." The fact is that under lagged reserve requirements a reduction in the monetary aggregates requires that the Federal Reserve allow the Federal funds rate to rise so that the banks can contract their loans and investments over a longer and more delayed period than is necessary under synchronous reserve requirements. The big "if" in the beginning of your staff's statement makes the sentence true,but not responsive to the widely held belief that supply related disturbances in the monetary aggregates are more difficult to control and require greater variability in the Federal funds rate than under a system of synchronous reserve requirements.

Even for keeping the Federal funds rate on target without reference to the target ranges for the aggregates you use, lagged reserve requirements cause the Federal funds rate to vary more than under synchronous reserve requirements. This is because the demand for bank reserves in the current week is less responsive to interest rates so that changes in the supply of reserves cause a bigger movement in interest rates (the supply curve shifts along a more inelastic demand curve). Professor William Poole presents evidence on this point in his article "Commercial Bank Reserve Management in a Stochastic Model: Implications for Monetary Policy", Journal of Finance (December, 1968, especially his table on pages 788-789).

The following alleged reason for the Federal Reserve's position on lagged reserve requirements was suggested by some of the experts. Although there is little question that lagged reserve requirements interfere with the conduct of monetary policy, the Fed thinks a change to synchronous reserve requirements may have some slight negative effect on membership since some banks may -- mistakenly -- view the lagged system as desirable. I do not think that the country's monetary policy should be jeopardized on such a pretext if, in fact, this is a reason for the Fed's position.

I think the evidence is overwhelming. Lagged reserve requirements do hinder monetary management and the Fed should immediately return to the system of synchronous reserve requirements used before September, 1968.

I think that the effect of reserve requirements on monetary control is sufficiently important to warrant an answer which directly addresses the literature cited above and the issues I have raised. Could you supply me with such a response as soon as possible so that we may study it before our July 26 hearings.

Sincerely,

Henry S. Reuss

Henry S. Reuss
Chairman

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

July 20, 1977

The Honorable Henry S. Reuss, Chairman
Committee on Banking, Finance and Urban Affairs
U. S. House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

I am pleased to reply to your letter of July 12 which deals with the issue of lagged versus synchronous reserve accounting.

Our staff has studied this subject intensively on a number of occasions in recent years. Their analysis has taken into account the various issues raised in the scholarly studies which you cite.

None of the evaluative work done by the Board's staff suggests that lagged reserve accounting seriously impedes the management of the monetary aggregates or contributes to disruptive money-market conditions.

I have, however, asked our staff to update their earlier studies and to make a new report to the Board. I shall see that their evaluation is also made available to you. It will not be possible, however, to complete that work before this month's oversight hearings.

With best regards,

Sincerely yours,

Arthur Burns

Arthur F. Burns

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

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WASHINGTON, D.C. 20515

225-4247

July 21, 1977

Dr. Arthur F. Burns
Chairman
Board of Governors
Federal Reserve System
Washington, D. C. 20551

Dear Dr. Burns:

Thank you for responding to my letter of July 12 on the subject of lagged reserve accounting which I believe to be important for short-run monetary management.

In your response, you say "None of the evaluative work done by the Board's staff suggests that lagged reserve accounting seriously impedes the management of the monetary aggregates or contributes to disruptive money-market conditions." (My emphasis.)

The list of experts I sent you, each of whom stated that the system of lagged reserves seriously impedes monetary management, contained economists who have been or are now with the Federal Reserve System, including the eminent staff of the Board: George Kaufman, formerly Assistant Vice President and Economist at the Chicago Federal Reserve Bank, William Poole, formerly Senior Economist of the Board of Governors and Assistant Vice President of the Boston Federal Reserve Bank, Albert E. Burger, Assistant Vice President of the Federal Reserve Bank of St. Louis, and R. Alton Gilbert, Economist of the Federal Reserve Bank of St. Louis. I would like to now add Daniel E. Laufenberg, currently on the staff of the Board, who, I notice, has published a comment in the May 1976 issue of the Journal of Money, Credit and Banking, which seriously attacks the short-run policy implications of lagged reserve requirements. In addition, Nobel Laureate, Milton Friedman's testimony before the Senate Banking Committee (November 4, 1975) "The most important single step at the moment in the regulations the Fed could take would be to eliminate its lagged reserve requirements," should not be ignored.

Accordingly, I would appreciate your making available the Board's staff studies on lagged reserve accounting, so that we can have a full background for the position you are taking, and an opportunity to obtain your views.

Sincerely,

Henry S. Reuss
Chairman

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

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BANKING, CURRENCY & HOUSING COMMITTEE

October 7, 1977

The Honorable Henry S. Reuss
Chairman
Committee on Banking, Finance
and Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Henry:

As I indicated in our earlier correspondence on lagged reserve accounting, I asked the staff to make another study of this question. A copy of their new study is enclosed.

The Board discussed the matter at length at two recent meetings. The view of the Board, which is supported by the staff, is that there would be no clear advantage in returning to contemporaneous reserve accounting.

I realize that you and some others have taken a different position. It may therefore be useful for you and me, perhaps with members of our staff, to sit down together and discuss the issues. Please let me know when such a meeting would be convenient.

With best regards,

Sincerely yours,

Arthur

Arthur F. Burns

Enclosure

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

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WASHINGTON, D.C. 20515

225-4247

November 7, 1977

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

Dear Dr. Burns:

One of the glaring problems confronting the American economy today, as you know, is the continuance of high interest rates, even while the money supply has for the last six months run far ahead of the top of your targets.

Instead of lower interest rates and increased investment, the intended results of a rapid growth in the money supply, the nation is experiencing a surge of corporate takeovers which does nothing for jobs or economic growth.

Rather than invest in new plant and equipment, businesses are using available cash and credit to buy up other companies at a rapid clip. Preliminary data show that corporate takeovers will hit a total of nearly 2,200 this year, a 50 percent increase over 1976, and the largest volume since 1973.

One factor encouraging takeovers rather than investment is that stock prices -- depressed by continuing high interest rates -- often make it more attractive for firms to buy out other companies than to expand their own operations.

It would be very useful if you could address yourself publicly as soon as possible to what is happening to the money supply, why the surge of money is not producing the intended result of lower interest rates, and what the Fed's plans for dealing with the situation are. A clear and complete explanation would go a long way toward restoring confidence in the economy.

There appear to be several reasons why the surge in the money supply -- 9.2 percent over the past six months compared to the Fed's target of 4 - 6.5 percent -- is not producing lower interest rates.

One is that the large U. S. banks are lending abroad at a fierce pace. The 317 large banks that report weekly to the Fed, banks which control 55 percent of total U. S. banking assets, increased domestic business loans during the first six months of 1977 by an annual rate of only 7 percent. For the same period, their overseas branches increased loans to foreign business borrowers at an annual rate of 15.6 percent.

In dollars, there was an increase in the amount of U. S. bank deposits lent to foreign business borrowers, through overseas branches, of approximately $5 billion -- funds that would otherwise have been available for lending to U. S. business.

Thus, the increase in the supply of loanable funds, which was spurred by fast money growth in the U. S., has lowered borrowing costs for foreign businesses instead of U. S. businesses. This simply helps foreign businesses undercut U. S. businesses in world competition.

U. S. banks lend abroad instead of at home partly because foreign branches are not subject to reserve requirements. Not having to hold reserves, the banks can lend out a greater proportion of their deposits and thus make more profit.

The growth in the monetary supply has given the public, especially the participants in the international and domestic financial markets, the impression that our central bank has lost control of the money supply. This has tended to depress stock and bond prices as well as the price of the U. S. dollar, leading people to hold more cash as their confidence about the future of our monetary policy is undermined. There are four aspects of short-run monetary management which have undermined the Fed's ability to control the money supply, all four of which could be, in large part, corrected. Therefore, it is essential that you also fully address these problems and publicly state how the Fed will rectify them. These are:

1. <u>Lagged Reserve Requirements</u>. According to experts inside and outside the Fed, short-run management of the money supply is made more difficult by pegging reserve requirements of the current week to deposits held two weeks earlier. Prior to September, 1968, reserve requirements were based on deposits during the current week. A return to the system of synchronous reserve requirements would make current short-run monetary management easier.

2. <u>Seasonal Adjustments</u>. Seasonally adjusted figures on the money supply are unreliable because the method of making the seasonal adjustments distorts the money series by mixing in seasonals with cyclical periodicities and altering the timing of the series. Newer statistical techniques for identifying and adjusting for seasonal periodicities are available and should be used.

3. <u>Discount Rate</u>. Maintaining a discount rate below the federal funds rate induces banks to borrow at the Fed's discount window and re-lend in the money markets, adding to the money supply and helping to defeat efforts to bring the money supply under control. The difference between the discount rate and the federal fund rate also amounts to a subsidy to the banks.

Increasing the discount rate to the level of the federal funds rate would end the incentive to banks to borrow and re-lend.

4. <u>Lack of Coordination</u>. Some of the huge bubbles in the money supply are the result of large outlays by the Treasury in a short period of time, such as Social Security payments. These payments should be determined in advance by the Fed so that offsetting actions can be taken in the money markets.

I will look forward to your explanation of these issues.

Sincerely,

Henry S. Reuss

Henry S. Reuss
Chairman

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

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WASHINGTON, D.C. 20515

April 18, 1978

The Honorable G. William Miller
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Miller:

I want to commend you on your appointment of an esteemed committee to study improvements in the seasonal adjustment procedures applied to the money supply data. This has been a subject in which I have been interested. It is one of the areas of monetary management that certainly needs immediate attention.

After all, the 7.8% increase in the basic money supply for 1977 (4th quarter 1976 to 4th quarter 1977) exceeded by 20% the maximum growth rate that the Federal Reserve announced it would adhere to. This wide miss undoubtedly created great uncertainty, especially in financial markets and on the international exchange, about the Federal Reserve's ability to control the United States money supply.

Another aspect of monetary control in which I have been interested concerns the Federal Reserve's lagged reserve requirement regulations which require banks to calculate their reserves on the basis of deposits held two weeks earlier. In testimony before the Senate Banking Committee (November 4, 1975), economist Milton Friedman said "the most important single step at the moment in the regulations the Fed could take would be to eliminate its lagged reserve requirements".

I have called the Federal Reserve's attention to Milton Friedman's comments and to the comments of many other economists, many of whom have been or are now with the Federal Reserve System. Their arguments have persuaded me that the Federal Reserve should immediately drop lagged reserve requirements and return to the system of synchronous reserve requirements used prior to September 1968.

The Federal Reserve replied to my request with a twenty-three page report containing an analysis of the effects of lagged reserve requirements (October 6, 1977).

I have asked some of the leading experts on this subject, who are not now on the Federal Reserve staff, to analyze this report. These experts are

Edgar L. Feige, Professor of Economics, University of Wisconsin, with collaboration of Robert McGee;

William Poole, Professor or Economics, Brown University and formerly Senior Economist at the Board of Governors and Assistant Vice-President at the Boston Federal Reserve Bank;

Dr. Warren L. Coats, Jr., whose doctoral dissertation at the University of Chicago was entitled "The September 1968 Changes in Regulation D and Their Implications for Monetary Control", and who also has published "Regulation D and the Vault Cash Game" in the Journal of Finance (June 1973). The latter article purports to show how banks can double count their reserves under the lagged reserve requirement system;

George G. Kaufman, John B. Rogers Professor of Banking and Finance, University of Oregon, formerly Assistant Vice-President and Economist at the Chicago Federal Reserve Bank.

I am forwarding copies of these experts' comments on lagged reserve requirements to you so that the Federal Reserve can have the benefit of their analyses.

I would also like to point out that a number of articles on lagged reserve requirements have been written by economists on the staff of the Board of Governors and the regional banks. You may want to look at their articles also. These economists who have been or are now with the Federal Reserve System include:

Albert E. Burger, Assistant Vice President of the Federal Reserve Bank of St. Louis;

R. Alton Gilbert, Economist of the Federal Reserve Bank of St. Louis;

Daniel E. Laufenberg, the Board of Governors;

Dr. Robert D. Laurent, Economist at the Federal Reserve Bank of Chicago.

I think the message from all of the economists I have listed above indicates that lagged reserve requirements make it more difficult for the Federal Reserve to manage our country's money supply. I, therefore, support the return to the system of synchronous reserve requirements used before September of 1968.

Sincerely,

Henry S. Reuss
Chairman

Enclosures

University of Wisconsin

DEPARTMENT OF ECONOMICS
SOCIAL SCIENCE BUILDING
1180 OBSERVATORY DRIVE

MADISON 53706

January 27, 1978

The Honorable Henry S. Reuss
Chairman, Committee on Banking,
Finance and Urban Affairs
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Reuss:

At the request of Robert Auerbach, my colleague Robert McGee and I have enclosed our comments on the Federal Reserve Board Staff report entitled, "Analysis of the Impact of Lagged Reserve Accounting."

The Board's staff report suggests that the sole positive effect of the adoption of the lagged reserve accounting (LRA) convention has been to reduce the net costs of reserve portfolio management for individual banks. This non-quantified, but seemingly modest benefit, must be weighed against the alleged problems which LRA has created for the overall implementation of monetary policy and thus for the economy as a whole. The report tends to either deny the existence of such problems as to minimize their importance where they are empirically found to exist. Thus the gist of the report is to advocate LRA on the basis of the sole cited benefit, which the report implicitly concludes outweighs the several disadvantages of LRA. In our view this conclusion is unwarranted on the basis of the analysis presented. A step by step analysis of the conclusions, (1) - (6), presented on pp. 1-3 of the report will show some of the problems with the report's conclusion that LRA should be maintained.

Conclusion (1) juxtaposes the benefit of required reserve foreknowledge against the cost of unexpected excess reserve moments. The increase in member bank borrowing and offsetting Open Market Operations which these unexpected excess reserve movements necessitate implies money market conditions are being smoothed by defensive open market operations to offset this harmful consequence of LRA. As conclusion (2) admits, this tendency for increased money market instability after 1968 has been successfully eliminated by "enlarged defensive open market operations". Since the desk manager eliminates the inconvenience banks would otherwise face from the LRA induced heightened volatility in the funds rate, it is no wonder that individual banks prefer LRA to CRA since it gives them the definite advantage of more efficient reserve management at a cost borne by the Fed.

This cost however is an important one because it means the Fed has an increased tendency to accommodate bank led credit expansion under LRA. A deposit created by a bank loan two weeks ago becomes validated M1-money if the Fed accommodates its creation by maintaining stable money market rates in the face of increased loan demand. If this is an effect of LRA, we would expect increased variability in the monetary aggregates which brings us to conclusion (3) in the report.

According to (3) the variability of M1 and M2 growth rates "was not affected by the introduction of lagged reserve accounting." Rather than disputing the analysis of the numbers presented in the staff report we offer, as prima facie evidence against this assertion, the following quote from the November 1971 Federal Reserve Bulletin, p. 880:

> Even when the revised data are examined, there is compelling evidence to suggest a marked increase in the variance of money supply and reserve innovations which coincided with the adoption of the amendment to Regulation D. (See Feige & McGree J.M.C.B. November 1977, p. 548).

With respect to the issue of the effects of LRA on the variability of the Federal funds rate, our own research revealed a standard deviation of weekly fund rate changes of .34 percentage points for the period 1961-1967 compared to .33 for the 1969-1975 period. We concluded that the effects of LRA on funds rate volativity has not been substantial when weekly changes are considered on a relative basis. While mean absolute changes have increased, variations around the mean are about the same for the pre- and post- LRA periods.

The Board's staff final three conclusions, (4) - (6), bear on the compatibility of LRA with current operating procedures (i.e. setting a funds rate through open market operations which is believed to be consistent with the desired monetary aggregate growth pattern). The conclusions reached are that 1) <u>given</u> current operating procedures it is a matter of indifference whether we have contemporaneous or lagged reserve accounting and 2) if a new operating procedure were adopted where reserves rather than the funds rate were controlled on a day to day basis, then lagged reserve accounting would be inferior to contemporaneous requirements because it would undermine the money-reserve relationship. This latter assertion is supported by the evidence presented on pp. 20-23 of the report which shows a deterioration in the money-reserve relationship after LRA was imposed. This is consistent with our finding in the JMCB article (Nov. 1977) which found the contemporaneous money-reserve relation disappears after the amendments to Regulation D were instituted.

Thus conclusion (6) minimizes the possible benefits to switching to a reserve operating procedure and contemporaneous reserve requirements. In addition a primary argument presented against such a policy is the increase in interest rate volatility which would result from using a reserve control rather than a funds rate control procedure. Once a reserve policy is regarded as unadviable it becomes largely a matter of indifference whether LRA or CRA is in force.

There are however arguments for a reserve operating procedure and against the allegation that it would increase interest rate fluctuations. Poole has argued persuasively, in "The Making of Monetary Policy: Description and Analysis" in the June 1975 issue of Economic Inquiry, that a reserve operating procedure should be adopted. Similarly, Professor Milton Friedman, in a "Statement on the Conduct of Monetary Policy" before the House Committee on Banking, Housing, and Urban Affairs on November 6, 1975, has argued that a reserve operating procedure rather than increasing interest rate changes would actually decrease them:

> The one serious objection to this procedure (controlling the stock of money) that I have seen is the contention that it would lead to more variability in interest rates over short periods than the present procedure. I have long believed that it would have precisely the opposite effect except possibly for very short periods measured in a few days or perhaps several weeks. By delaying interest rate adjustment, the present procedure permits pressure to cumulate. I believe that it thereby produces more erratic and unstable interest rates and therefore more uncertainty than the alternative procedure.

An additional benefit of the improved money control resulting from a reserve control operating procedure would be reduced inflationary expectations which many economists now realize are an important determinant of interest rate changes. Thus there is some consensus among economists that direct reserve control would result in tighter control over the money supply.

In our own research, we estimated a simple dynamic money market model including reserves, the money supply and the Federal funds rate for the 7 year period prior to LRA and the 7 year period after monetary aggregate targets were adopted in early 1970. We examined two issues. First, we analyzed the effect of LRA on the model, and secondly, we examined the data for evidence of a shift from control of interest rates to control of the money supply. While the early period model was consistent with the view of a monetary policy operating procedure which maintained stable interest rates by letting the money supply adapt to changes in money demand, the latter period was consistent with elements of both money and funds rate control policies.

Mr. R.

There is evidence that the Fed. now lets the funds rate adjust to bring money demand changes in line with the desired money supply. We also found evidence that reserves are being supplied to accommodate two week prior changes in money. This is consistent with the Board's staff report comment that defensive open market operations have increased as a result of LRA to offset latent instability in excess reserve and funds rate movements. LRA appears to be interfering with the Fed's ability to control the money supply because it necessitates increased defensive open market operations aimed at stabilizing interest rates which can only be accomplished by sacrificing some degree of control over monetary aggregates.

In summary, while LRA appeared to be a sensible procedure in the period of primary attention to money market conditions, it is inconsistent with a regime of monetary aggregate control. The simple explanation for this finding is that individual banks have a two week lead time in which to create however much money the public wants at current interest rates (i.e. money demand gets the jump on money supply). If interest rate targets to control money are not modified as it becomes necessary, then periods of undesirable money growth will either have to be tolerated or offset by appropriate open market actions. The more uncertain the Fed is about the appropriate interest rate target and the longer it allows the wrong funds rate target to persist, the more drastic and potentially destabilizing will be the corrective monetary policy.

Finally, regardless of whether or not LRA is abolished, the Federal Reserve's ability to control the money supply is likely to be enhanced if non-member banks are given sufficient incentives to join the System. LRA is such an incentive. More useful incentives can and should be developed.

I hope these comments will be useful for your evaluation of current policies and if I can be of any further help, please do not hesitate to contact me.

Sincerely yours,

Edgar L. Feige

Edgar L. Feige
Professor of Economics

/aw

BROWN UNIVERSITY Providence, Rhode Island - 02912

November 23, 1977

The Honorable Henry S. Reuss, Chairman
Committee on Banking, Finance and Urban Affairs
House of Representatives
Washington, D. C. 20515

Dear Congressman Reuss:

I am writing in response to your request for my evaluation of the Federal Reserve's position on lagged reserve requirements. Since this position is explained fully in the Federal Reserve Board's Staff Study, "Analysis of the Impact of Lagged Reserve Accounting" (October 6, 1977), a copy of which you sent to me, I will make frequent reference to this document.

In general, I have little quarrel with either the theory or the evidence presented in the Staff Study. However, the Staff Study contains several unsupported and misleading statements and, more importantly, conclusions that do not follow from the theory and evidence presented. In my view, the Staff Study actually strengthens the case against lagged reserve accounting ("LRA" for short).

<u>LRA under current operating procedures</u>. For many years the Federal Reserve's operating procedures have involved tight control of the federal funds rate on a day-by-day basis. Given that the federal funds rate is tightly controlled, the Staff Study correctly argues that, "short run movements in the [monetary] aggregates are largely demand determined. It is difficult to argue that lagged reserve accounting has much relation to the public's demand for money" (p. 14).

It is worth noting in passing that this argument, at least to a very close first approximation, extends to <u>all</u> aspects of the reserve requirements system, including not only LRA but also reserve requirements differentials between banks of different sizes and the complete lack of Federal Reserve reserve requirements on non-member banks. Thus, it is inconsistent of the Federal Reserve to oppose reform of LRA and at the same time to favor extension of reserve requirements to non-member banks for monetary control purposes.

What, then, are the advantages of LRA given the Federal Reserve's current operating procedures? In the Record of Policy Actions of the Board of Governors for April 23, 1968 the introduction of LRA (effective September 12, 1968) was explained as follows:

> The amendments were designed to facilitate more efficient functioning of the reserve mechanism. They did not represent any change in Federal Reserve monetary policy, but were expected to reduce uncertainties, for both member banks and the Federal Reserve, as to the amount of reserves required to be maintained during the course of any reserve-computation period. Adoption of the amendments was therefore expected to moderate some of the pressures for reserve adjustments within the banking system that occasionally develop near the close of a reserve period and produce sharp fluctuations in the availability of day-to-day funds." (Board of Governors of the Federal Reserve System, Annual Report 1968, p. 82.)

The Staff Study makes clear that LRA did not in fact "facilitate more efficient functioning of the reserve mechanism." The Staff Study nicely documents the fact that, "the volatility of money market conditions toward the end of the statement week -- as measured by variations in member bank borrowing, the Federal funds rate, and open market operations -- showed a marked tendency to increase immediately after the rule change." (Staff Study, p. 8, emphasis added).

The cost of this increase in volitility was not borne by the banking system alone, but also by the Federal Reserve and, therefore, indirectly by American taxpayers. Because the 1968 changes made the money markets more volitile the Federal Reserve has felt compelled to engage in more extensive defensive open market operations. "The Manager of the Trading Desk's outright transactions as a percentage of total reserves remained virtually unchanged, but the volume of matched sale-purchase and repurchase agreements as a percentage of total reserves doubled immediately following the rule change and remained in the higher range through 1972." (Staff Study, p. 9, emphasis added). The Staff Study provides no estimate of the cost of the extra open market operations, but it is obvious that some extra and completely unnecessary Federal Reserve costs were generated by the rule change.

The Staff Study argues that two benefits were realized from the rule change. The first is that, "the evidence clearly suggests that in one important sense bank reserve management has been more efficient under the new rules. The average value of member bank excess reserves declined from $368 million in 1967 to $192 million by 1970. The improved reserve management, however, probably results entirely from the extension of the carryover privilege to include surpluses." (Staff Study, p. 6, emphasis added.) I have no reason to dispute the Staff's conclusion; indeed, I have on a number of occasions argued for expanded carryover privileges. In any event, the LRA part of the new rules was not responsible for the claimed benefit.

The second claimed benefit is that LRA reduces bank costs of reserve management. "A survey in 1975 of commercial bank Directors of Reserve Banks, and branches suggested that...most banks believed their reserve management was improved by lagged accounting and felt that a return to contemporaneous accounting would increase costs, mainly from additional staffing." (Staff Study, p. 7). The evidence offered for this claim is very weak. Commercial bank Directors of Federal Reserve Banks and branches rather than bankers in general were surveyed. The number of bankers surveyed could not have exceeded 50 or 60 out of some 5000 member banks, and bankers serving as Federal Reserve Directors are unlikely to be a representative sample of all bankers. Moreover, the Staff Study contains no tables reporting survey responses to show that the bankers favoring LRA were a large majority of those surveyed or that the bankers felt very intensely about the issue. Finally, information obtained from even a properly designed survey on this matter must be regarded with suspicion because many bankers who understand the impact of regulations on their individual banks fail to understand the impact of regulations on the banking system as a whole.

To summarize the Staff Study's analysis of LRA under current Federal Reserve operating procedures, the only advantage of LRA is that an unknown number of bankers apparently feel that LRA reduces their costs of reserve management. On the cost side of the ledger, the Staff Study presents a well-documented case that LRA has led to some combination of greater short-run interest rate instability and larger defensive open market operations. Finally, LRA has little or nothing to do with money stock control so long as current operating procedures are maintained.

LRA under a reserves operating procedure. Along with many other economists, I have advocated reform of the Federal Reserve's operating procedures so that the Open Market Desk would stabilize bank reserves rather than the federal funds rate on a day-to-day basis. The arguments for this reform go far beyond the scope of this letter and, except to note that reserves control can be expected to provide better control over the monetary aggregates than is now possible, will not be discussed here. However, there is widespread agreement that if this reform were put in place, then it would be highly desirable to substitute contemporaneous for lagged reserve accounting.

If the Federal Reserve were to control bank reserves on a day-to-day basis, then contemporaneous reserve accounting would be desirable because the accuracy of money stock control would be improved as compared to the LRA system. The Staff Study supports this argument. "Empirical evidence on the linkage between monetary and reserve aggregates indicates a closer -- though still relatively loose -- relationship before the institution of lagged reserve accounting than after." (Staff Study, p. 20). "If the Manager were instructed to focus on attaining a reserve aggregate target in his daily operations, a return to contemporaneous accounting implies less short-term variability of deposits and monetary aggregates than would be the case with lagged accounting." (Staff Study, p. 23).

The Staff Study also accepts the argument that under a reserves operating policy LRA would generate larger interest rate fluctuations than would contemporaneous reserve accounting. "[Following a rise in deposits] ... under lagged reserve accounting there is no change in bank demands for reserves and no automatic pressure on money market rates for two weeks, thus delaying this automatic offset. Moreover, because of the delay, interest rates would have to rise to higher levels over time to achieve a given average level of money over a particular period." (Staff Study, p. 23).

To summarize the Staff Study's analysis of LRA under a reserves operating policy, LRA would make both the money stock and interest rates more volitile than would contemporaneous reserve accounting. Set against these costs would be, presumably, the alleged lower costs of bank reserve management discussed earlier. However, although the Staff Study does not discuss this point, my guess is that the authors of the Study would agree that the banks' costs from the greater interest rate variability under LRA as compared to contemporaneous reserve accounting would not be offset by the computational ease of LRA.

<u>General comments</u>. The Staff Study includes several statements that are misleading with respect to the LRA issue. First, the Study says that, "any reduced variability in the monetary aggregates that may result from [a reserves] operating procedure, when compared to the present one, would come at the expense of unprecedented short-run variability in the funds rate." (Staff Study, p. 23). This statement is misleading because the issue at hand is LRA rather than a reserves operating procedure. The Staff Study agrees that except for possible benefits to banks flowing from ease of reserves management under LRA, contemporaneous reserve accounting is better under <u>either</u> the current Federal Reserve operating procedures <u>or</u> a reserves operating procedure.

Second, the Staff Study gives the impression that the proposal for a reserves operating procedure ought not to be taken seriously. "Contemporaneous accounting would only be advantageous under alternative operating procedures, for example, one in which the [Federal Open Market] Committee instructs the Manager to attempt to hold each week to some predetermined target path for a reserve aggregate like nonborrowed reserves -- letting the funds rate move freely. All of the academic studies of the effects of lagged accounting on monetary control have examined such a hypothetical case." (Staff Study, p. 19).

Regrettably, it is quite clear that the Federal Reserve has indeed regarded a reserves operating procedure as nothing more than a "hypothetical case," not to be taken seriously. This attitude has been unfortunate, but is now doubly so in the light of a recent court decision whose implications for this issue are not widely understood.

On November 10, 1977 the Federal Appeals Court in Washington, D.C. ruled that under the federal Freedom of Information Act the Federal Reserve is required to release its decisions sooner than has been its recent practice. (See the newspaper account in the November 11, 1977 Wall Street Journal.) Moreover, it was reported in a New York Times article on November 17, 1977 that the Solicitor General may not seek a Supreme Court review of the Appeals Court decision. Without expressing opinion one way or the other on this case, I can merely note that the Federal Reserve may shortly be required to release its decisions promptly, and that the Federal Reserve ought to be examining with considerable urgency the consequences of this requirement.

The most obvious consequence of earlier release of Federal Reserve decisions is that one aspect of the Federal Reserve's current operating procedures will have to be changed. The Federal Open Market Committee will no longer be able to instruct the Manager to change the federal funds rate in small steps over a period of weeks because public release of such an instruction will produce an immediate market reaction as market participants attempt to realize the gains or avoid the losses implied by announced interest rate changes.

The importance of earlier release of Federal Reserve decisions should not be underestimated. The Federal Reserve will be driven to changing the federal funds rate in discrete steps immediately following Open Market Committee meetings, and one of the main claims for the current operating procedures -- that of smooth and "orderly" changes in money market interest rates -- will no longer be valid. More importantly, however, earlier release of Federal Reserve decisions is likely to lead the Federal Reserve to change its interest rate targets less often which will make the money stock even more unstable and procyclical than it has been in the past.

These problems could be handled if the Federal Reserve were to adopt a reserves operating policy, a reform that is desirable in any event. Since the Federal Reserve has not, to the best of my knowledge, engaged in any planning for a reserves operating procedure, I strongly urge the House Banking Committee to request that the Federal Reserve conduct a study to determine what needs to be done if a reserves operating procedure is to be adopted.

It should be clearly understood that the LRA issue is only part of the much larger issue of how to structure Federal Reserve regulations to ensure that a reserves operating procedure functions as smoothly as possible. In a number of places the Staff Study refers to the role of the current operating procedures in preventing supply-side disturbances from affecting the money stock, but what the Staff Study does not mention is that many of these supply-side disturbances are a direct result of the reserve requirement regulations, such as LRA, the Federal Reserve has adopted. However, the Staff Study shows that the Federal Reserve does recognize the importance of reserve requirement regulations in general. "The introduction of graduated reserve requirements and a more complicated reserve structure in the 1970's may also have weakened the short-run reserve-money relation, but our evidence so far suggests that lagged reserve accounting had a stronger negative impact." (Staff Study, p. 21).

In closing, let me say that it is very encouraging that the Congress has become interested in monetary control issues, but I feel that it is unfortunate that this interest has extended to an issue as technical as LRA. I fully understand that this situation arose because LRA is a well-defined and specific issue and because academic experts have mentioned this issue so often. But I am certain that most academics would agree with me that LRA is only part of the much larger issue of designing regulations better suited for monetary control.

I suggest, accordingly, that the Banking Committee request the Federal Reserve to provide a study of recommended regulatory changes based on the assumption that a reserves operating procedure is to be adopted. It is important that this study be based on the <u>assumption</u> that a reserves operating procedure is to be adopted; only after the completion of this study, and receipt of informed comment on it, will be possible to judge the adequacy of the Federal Reserve's position on the relative merits of the money market and reserves operating procedures against the background of the Federal Reserve having actually investigated what a reserves procedure would entail.

If I may be of any further assistance, please feel free to call on me again.

Sincerely,

William Poole

William Poole
Professor of Economics

WP/md

[redacted]
Arlington, Virginia 22202

November 7, 1977

The Honorable
Henry S. Reuss
Chairman, Committee on Banking,
Finance and Urban Affairs
U.S. House of Representatives
Washington, D.C. 20510

Dear Mr. Reuss:

It is my pleasure to respond to your Committee's request for comments on "Analysis of the Impact of Lagged Reserve Accounting" prepared by the staff of the Board of Governors of the Federal Reserve System earlier this month. I do so as a student of U.S. monetary policy and central banking and, in particular, of lagged reserve accounting. I am acting in an entirely personal capacity, and request that the name of my current employer not be used in connection with these comments.

Chairman Burns has carefully stated that "there would be no clear advantage in returning to contemporaneous reserve accounting." In this he is supported by the above-mentioned staff report. While Chairman Burns is correct that the evidence has not yet clearly established the advantage of a return to contemporaneous reserve accounting, it is equally true that there is no evidence indicating net disadvantages to such a return and a fairly strong theoretical case that there would indeed be some important advantages.

The report itself maintains the high standards of scholarship I have come to expect of the Board's staff. By and large, it is an updating of the analysis and statistics contained in my doctoral dissertation written at the University of Chicago over five years ago. The report does find, as had my dissertation, a significant loosening of the relationship between reserves and deposits since the introduction of lagged reserve accounting.

The staff's defense of the harmlessness of lagged reserve accounting rests on two propositions. First, the use of a federal funds rate operating target makes reserves endogenous to demand-determined deposit levels. In this setting, an increase in reserves that would lead to a greater deposit expansion under lagged reserve accounting than under concurrent reserve accounting cannot occur in the first place without a shift in the demand for deposits or a change in the federal funds rate target. Second, in the most interesting empirical study of the money supply control aspects of lagged reserve accounting I have seen to date (John Judd's work for the Federal Reserve Bank of New York), the estimated interest elasticity of deposit demand was found to be smaller in the short run than the supply elasticity.

These interest rate estimates imply that, even with a reserve aggregate operating target, lagged reserve accounting will not have very significant practical consequences for monetary control, because the tendency for deposits to rise in the face of an increase in reserves will be quickly dampened by a falling federal funds rate, while the demand for deposits will be only insignificantly increased. As a result, deposits will change only insignificantly in the very short run and as it is changes in deposit levels that introduce the differing impact between lagged and contemporaneous reserve accounting, the empirical magnitude of the difference will itself be negligible. It is this reasoning that leads to the conclusion that lagged reserve accounting will not significantly affect the behavior of the federal funds rate, even when the funds rate target must be adjusted in order to meet the money supply target. It is precisely at such times, as for example when maintaining the federal funds rate target leads to unexpectedly large increases in reserves and deposits that must be reversed if money supply objectives are to be met, that lagged reserve accounting potentially gives the most trouble. But if the short-run elasticity of deposit demand is very small relative to the short-run elasticity of deposit supply, a very modest increase in the federal funds rate will reestablish the desired money supply.

The staff's logic to this point is unassailable, but the evidence underlying it is highly questionable. Judd's empirical results are highly sensitive to at least two questionable assumptions. First is his assumption that the use of the federal funds rate as an operating target makes it totally exogenous in his estimated money demand function. This means that none of the movements in federal funds rate are attributable to changes in the supply of money, while in fact the rate is allowed to fluctuate within a narrow band. In a very preliminary reexamination of Judd's generally praiseworthy work on this subject, colleague Iqbal Zaidi of Princeton University and I have found that relaxing this assumption (by assuming that the Fed adjusts the federal funds rate, when actual money growth rates deviate from the Fed's targeted rates) more than doubles the elasticity of demand estimate over the one found by Judd. This increases the variation in deposits that can take place within a single week and thereby increases the practical significance of the theoretically well-known instability introduced by lagged reserve accounting.

We have yet to determine the sensitivity of these elasticities to Judd's assumption that deposit supply is totally demand determined. In our view, deposits do not expand in the first instance because the public desires a higher level of deposits, but rather as the indirect consequence of the public's increased demand for loans. This introduces an exogenous supply element in the determination of deposits. To the extent that this view is valid, Judd's demand function, which only permits lagged adjustment of deposits to changes in their demand, is misspecified and most likely biases his estimated elasticity of demand downward. I regret that our work is not further advanced at this point.

In conclusion, it is my view that the assertion of lagged reserve accountings' harmlessness is based on a mistaken view of the money supply process, which pictures it as wholly demand determined and of the highly questionable statistical estimates that have resulted from models reflecting this view. I am still inclined, subject to further investigation of the evidence, to the view that lagged reserve accounting has significantly increased the variations in the federal funds rate necessary to bring monetary growth into line with the Federal Reserve's own targets whenever such growth deviates from those targets. As a consequence of this and the Federal Reserve's adherence to a federal funds rate operating target, the money supply has become more difficult to control and has tended to wander from its targeted levels by wider margins and over longer periods of time with greater pressure on federal funds rates than would have been experienced under concurrent reserve accounting.

Sincerely,

Warren L. Coats, Jr.

Warren L. Coats, Jr., Ph.D.
Economist

October 16, 1979

The Honorable Paul E. Tsongas
Chairman
Consumer Affairs Subcommittee
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Tsongas:

I am pleased to enclose the attached responses to the additional questions relayed by telephone subsequent to your September 26 letter.

Should you or your staff have any questions regarding the attached responses, please contact Jeanine Catalano, Review Examiner, at (202) 452-3946.

Sincerely,

S/ Paul

Enclosures
JC:smk (V-47)
bcc: Jeanine Catalano
Mrs. Mallardi(2)

14. What is your policy on the number of violations identified before an institution is required to do its own file search?

When a violation is discovered using the statistical sampling procedures, additional loan files are selected judgmentally to determine the cause of the violation and the existence of a pattern. In cases where it is determined a pattern exists, such as a certain loan type or loans made by a certain loan officer. file searches for those particular types of transactions are required. In cases involving isolated errors, where no pattern is detected, banks are required to conduct a file search.

15. In how many cases has the Federal Reserve Board required institutions to perform file searches?

The response to this question will be included in the responses to your letter dated October 5, 1979.

16. In those cases were institutions have done file searches, what have been the results? How did the Federal Reserve Board verify the validity of the results?

In comparing the actual reimbursements made after file searches were conducted to estimates provided by examiners, we have noticed differences between the amounts reimbursed and the estimated dollars of overcharges. In some cases, more than the estimated amount was reimbursed; in others, less. Results of the file searches are ultimately verified by spot testing by the examiner during the next examination. As indicated in our response to your earlier question 13, the Reserve Banks utilize follow-up procedures such as telephone calls, letters and reviews of file search procedures to ascertain completeness of State member bank corrective action.

CM

October 31, 1979

The Honorable Benjamin S. Rosenthal
Chairman
Subcommittee on Commerce, Consumer
and Monetary Affairs
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Chairman Rosenthal:

As indicated in my letter to you of October 18, I am pleased to enclose the report received from the Federal Reserve Bank of Cleveland concerning the clearance of a bank draft drawn on an Irish bank in pounds.

I believe you will find this report self-explanatory. Please let me know if I can be of further assistance.

Sincerely,

S/Paul A. Volcker

Enclosure
CO:pjt (#V-78)
bcc: Jack Ryan

Action assigned Jack Ryan

Congress of the United States
House of Representatives
COMMERCE, CONSUMER, AND MONETARY AFFAIRS SUBCOMMITTEE
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS
RAYBURN HOUSE OFFICE BUILDING, ROOM B-377
WASHINGTON, D.C. 20515

October 15, 1979 #78

Hon. Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C. 20551

Dear Mr. Chairman:

Enclosed is a copy of a letter I have received from a citizen who is having trouble getting clearance of a bank draft drawn on an Irish bank in pounds. A copy of the bank draft is also enclosed. On the surface it would appear that Mr. O'Neill is not being fairly treated by the banking system, and I am writing to request the assistance of the Federal Reserve on this matter.

In particular, does Mr. O'Neill have a legitimate complaint? What factors could reasonably be expected to cause this much delay in securing clearance of such a bank draft?

Also, is there any assistance that the Federal Reserve can provide to straighten out this situation for Mr. O'Neill?

Sincerely,

Benjamin S. Rosenthal
Chairman

BSR:tv

Enclosures 2

[redacted]
September 25, 1979

Representative Benjamin Rosenthal
Chairman Commerce Subcommittee of the
House Governmental Operation Committee
Room 2372 Rayburn House Office Building
Washington, D. C. 20515

Dear Sir:

It has recently come to my attention that your subcommittee is interested in the delay in the check clearing process.

I am currently involved in a check clearing dilemma that I would like to call to your attention.

On August 6, 1979 I received a check from a bank in Northern Ireland, payable to me and denominated in pounds. I took this check to the foreign department of the First National Bank of Cincinnati. They refused to handle it because I did not have an account there. I then took the check to the Provident Bank in Cincinnati where I do have an account. They agreed to accept the check for collection and forwarded it to the Chemical Bank of New York on which it was drawn. I am still waiting for this check to clear. The only thing the Provident Bank tells me is that when the check clears they will let me know.

I feel that I am the victim of some kind of a national and international confidence game in which my money is being used by the banking system to buy gold at my expense. In the meantime, the value of the pound has been falling drastically against the dollar. The value of this check has fallen about 10% since it has entered the clearing process.

Any help your subcommittee can render the banking system in general, and to me in particular, to cure this type of shenanigans will certainly be appreciated by all.

Very truly yours,

Frank O'Neill

Frank O'Neill

Enc. Copy of check.

ALLIED IRISH BANKS LIMITED
8 High Street, Omagh, Co. Tyrone.

26th July, 1979.

PAY TO THE ORDER OF Francis O'Neill Esq.,

THE SUM OF Three thousand nine hundred and fifty one pounds sixty seven pence.--- £3,951.67

TO:

The Chemical Bank,
20 Pine Street,
New York.

Initials

FOR ALLIED IRISH BANKS LIMITED

MANAGER

[redacted]

October 31, 1979

The Honorable Henry S. Reuss
Cochairman
Subcommittee on International Economics
Joint Economic Committee
Washington, D. C. 20510

Dear Henry:

Thank you for your letter of October 26 regarding the Subcommittee on International Economics' field hearing in New York City focusing on the domestic and international implications of the Federal Reserve's monetary policies.

I am pleased to inform you that Governor Henry C. Wallich will testify on behalf of the System on November 5 at 9:00 a.m. Governor Wallich will be accompanied by Scott Pardee.

Sincerely,

S/Paul A. Volcker

CO:vcd (#V-102)
bcc: Gov. Wallich
Mr. Axilrod
Mr. Truman
Mrs. Mallardi (2)

Chairman will be [illegible]scussing with Governor Wallich. Info copies given Messrs. Axilrod & Truman

Co...

(C...

WASHINGTON, D.C. 20510

October 26, 1979

1979 OCT 30 10:58

#102

Mr. Paul A. Volcker
Chairman
Board of Governors
Federal Reserve Board
Constitution Avenue
Washington, D.C. 20551

Dear Chairman Volcker:

On November 5, 1979, the Joint Economic Committee's Subcommittee on International Economics will be holding a field hearing in New York City focusing on the domestic and international implications of the Federal Reserve's monetary policies. As Cochairman of the Subcommittee, I would like to extend at the request of Senator Jacob K. Javits an invitation to Mr. Scott Pardee, Vice President in the Foreign Function of the Federal Reserve Bank of New York and Deputy Manager of Foreign Operations of the System Open Market Account, to testify before us at this hearing. The hearing will begin at 9:00 a.m. in Room 305C, 26 Federal Plaza.

Mr. Pardee's intimate knowledge of foreign exchange markets and his thorough understanding of both foreign and domestic intervention operations make him a particularly attractive witness. He could add immeasurably to our own understanding of the international implications of recent Federal Reserve policy initiatives.

I hope that you give leave to Mr. Pardee to testify before us on November 5. I look forward to your early reply.

Sincerely,

Henry

Henry S. Reuss
Cochairman

October 31, 1979

The Honorable Walter D. Huddleston
United States Senate
Washington, D. C. 20510

Dear Senator Huddleston:

Thank you for your letter of October 22 requesting our comments on the inquiry from Mr. Edward L. Cawood regarding the fees charged to the Bank of Harlan by the Cincinnati Branch for the late reporting of receipts of Federal tax deposits.

Treasury Department regulations require that Federal Reserve Banks, as fiscal agents for the Treasury, charge remittance option banks a fee whenever their reports of Federal tax deposits are not received at the Reserve Banks by the next business day after the taxes are deposited. The Treasury's regulations make no distinction regarding the means by which the reports are delivered; all reports must be received by the next business day. This one-day remittance requirement has generated a considerable amount of comment in the banking industry. If Mr. Cawood has any additional comments or questions regarding this matter, we suggest that he write to:

Mr. Paul H. Taylor, Fiscal Assistant Secretary
Department of the Treasury
1500 Pennsylvania Avenue, N. W.
Washington, D. C. 20220

We contacted the Cincinnati Branch regarding an earlier inquiry on Mr. Cawood's behalf and were advised that an officer from the Branch has recently discussed with the Bank of Harlan the various ways that Federal tax deposit reports can be forwarded in order to insure timely delivery. We were also advised by Cincinnati that the Bank of Harlan has worked out an arrangement with the Postal Service whereby the Bank will be able to submit its reports within the time limits and no longer incur late fees.

Sincerely,

S/Paul A. Volcker

(DD:JPB:)vcd (#V-101)

bcc: Mrs. Mallardi (2)

WALTER D. HUDDLESTON
KENTUCKY

Will be handled by Congressional
Liaison office

United States Senate

WASHINGTON, D.C. 20510

SELECT COMMITTEE ON
SMALL BUSINESS

#101

October 22, 1979

Chairman Paul A. Volcker
Chairman
Federal Reserve Bank
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Chairman Volcker:

Enclosed is a copy of a letter I have received from Edward Cawood, Chairman of the Bank of Harlan in Harlan, Kentucky.

Mr. Cawood complains of excessive charges to his bank for receipt of taxes by the Cincinnati Federal Reserve Bank beyond deadline dates. Mr. Cawood claims these charges are extended unfairly because the checks arrived late due to circumstances beyond their control.

I would appreciate your comments on Mr. Cawood's complaints, and information on what, if anything, is being done to alleviate the situation.

Thank you for your assistance in this matter.

Sincerely,

Walter D Huddleston

Walter D. Huddleston

THE BANK OF HARLAN

HARLAN KENTUCKY 40831

[illegible] EVERSOLE
[illegible]

[illegible] SECURITY OFFICER

ANN E. BLESSING
ASST. CASHIER

August 29, 1979

Honorable Walter D. Huddleston
[illegible] Dirksen Senate Office Building
Washington, D. C. 20510

Dear Senator Huddleston:

We wish to solicit your aid in ending the most unfair and uncalled for action this bank has ever suffered in my forty-five years in the banking industry through the Federal Reserve Bank, which in turn attributes the injustice to the Treasury Department.

In the course of our collection of government withheld taxes from our customers, from which we receive not one cent in income, we send each one the day we receive it by first class mail to the Federal Reserve Bank in Cincinnati. Certain days due to postal service or red tape in the Reserve Bank, the letter evidently does not arrive the next day as expected; so we are fined for being late. On Saturdays I understand the Federal Reserve Bank is closed, and we are charged interest for Saturday and Sunday.

To improve the situation, we have tried Purolator service; but the remittance still sometimes arrived late. Moreover, the Purolator service charged us $4.76 to transmit a letter to Cincinnati. This is too much to pay for remitting our collection of the government's taxes.

We have called the President of the Federal Reserve Bank. Yesterday the Fed finally agreed to correct their mistake of $100,000.00, on which they had assessed us $203.00. We had to call the President of the bank, as in the lower echelon the answer was that there was nothing that could be done.

We have been charged the last three months approximately $200.00, $500.00 and $718.00 less $203.00 promised credit. It is outrageous to think that our government would charge us such amounts to collect its taxes.

We have called the Kentucky Bankers Association and Mr. Moremen, and he promised to talk to one of our Senators.

We are enclosing Xerox copies of our July charges.

Honorable Wendell H. Ford
August 29, 1979
Page Two

We wish it were possible that we did not have to collect withheld taxes but feel compelled to help our customers. We would appreciate your help in correcting this "rip off" by government.

Best wishes to you.

Respectfully yours,

Edward L. Cawood

Edward L. Cawood
President

ELC:jy

Enclosure

[illegible] BANK OF HARLAN
FIRST & CENTRAL ST
HARLAN KY 40[illegible]

ACCOUNT NO 0421-0760-[illegible]

REMIT CLASS 1 | DATE 08/27/79

[illegible] TAX AND LOAN STATEMENT

[illegible] SUMMARY

THE FOLLOWING STATEMENT SUMMARIZES THE [illegible] USED TO CALCULATE LATE ADVICE CHARGES AND REIMBURSEMENT FEES WHICH ARE TO BE DEBITED AND/OR CREDITED TO YOUR RESERVE ACCOUNT OR YOUR MEMBER [illegible] RESERVE ACCOUNT

LATE ADVICES RECEIVED DURING REPORT CYCLE
07/05/79 THRU 08/0[illegible]/79

ADVICE DATE	ENTRY DATE	RECEIVE DATE	T&A CODE	REPORT CYCLE MO WK	DAYS LATE	DAILY RATE	ADVICE AMOUNT	LATE CHARGE
07/05	07/06	07/09	02	07 1	3	.00028	[illegible],[illegible]03.03	45[illegible]
TOTAL ADVICE LATE CHARGE								45[illegible]
07/09	07/10	07/11	02	07 [illegible]	1	.00028	[illegible],799.02	[illegible]
TOTAL ADVICE LATE CHARGE								[illegible]
07/27	07/28	07/19	02	07 2	1	.00028	5,[illegible]66.38	[illegible]
TOTAL ADVICE LATE CHARGE								[illegible]
07/30	07/[illegible]	08/01	02	07 4	[illegible]	.00029	[illegible].50	[illegible]
TOTAL ADVICE LATE CHARGE								[illegible]
07/25	07/26	08/03	02-2	07 4	7	.00029	100,000.00	203.00
TOTAL ADVICE LATE CHARGE								203.00
GRAND TOTAL								7[illegible]

LATE ADVICE CHARGE AND REIMBURSEMENT SUMMARY

NUMBER OF FTD'S PROCESSED BY IRS	[illegible]9	
FTD FEE RATE	0.[illegible]0	
TOTAL FTD CREDIT		109.50
TOTAL RESERVE ACCOUNT CREDIT ON 08/27/79		109.50
TOTAL RESERVE ACCOUNT CHARGE ON 08/27/79		71[illegible].72

October 30, 1979

The Honorable William S. Moorhead
House of Representatives
Washington, D.C. 20515

Dear Bill:

I appreciated your note of October 26 enclosing the letter and ad from Equibank.

These are difficult days and the support our program is receiving is encouraging.

Sincerely,

S/Paul A. Volcker

KAG:pjt (#V-99)
bcc: Mrs. Mallardi (2)

BARBER B. CONABLE, JR.
NEW YORK, 35TH DISTRICT

COMMITTEES:
WAYS AND MEANS
BUDGET
JOINT COMMITTEE ON TAXATION

Congress of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
237 CANNON HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-3615

DISTRICT OFFICE:
311 FEDERAL OFFICE BUILDING
100 STATE STREET
ROCHESTER, NEW YORK 14614
(716) 263-3156

October 8, 1979

Honorable Paul A. Volcker
Chairman
Federal Reserve Board
Constitution Avenue & 20th Street, N.W.
Washington, D.C. 20551

Dear Paul:

I want to encourage you to do the sort of things that were announced this weekend at the Fed. I know you'll get some flack from it, but there are people here in Congress who believe a little monetary courage is needed and who have great confidence in your ability to do what's necessary.

I shall continue to be grateful for your willingness to take on a thankless job at a difficult time and at what I am sure must be a considerable personal sacrifice to you and your family.

Sincerely,

Barber

Barber B. Conable, Jr.

C/l

Congressional Liaison office will draft response.

WILLIAM S. MOORHEAD
PENNSYLVANIA
14TH DISTRICT

WASHINGTON OFFICE:
2467 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-2301

MOLLIE D. COHEN
ADMINISTRATIVE ASSISTANT

PITTSBURGH OFFICE:
2007 FEDERAL BUILDING
PITTSBURGH, PENNSYLVANIA 15222
PHONE: 644-2870

NATHANIEL SHORE, ESQ.
PITTSBURGH ASSISTANT

Congress of the United States
House of Representatives
Washington, D.C. 20515

COMMITTEES:
BANKING, FINANCE AND URBAN AFFAIRS
CHAIRMAN, SUBCOMMITTEE ON ECONOMIC STABILIZATION
JOINT ECONOMIC COMMITTEE
CHAIRMAN, SUBCOMMITTEE ON FISCAL AND INTERGOVERNMENTAL POLICY
GOVERNMENT OPERATIONS

PENNSYLVANIA REGIONAL WHIP

WILLIAM R. MALONI
SPECIAL ASSISTANT

October 26, 1979

#99

Honorable Paul A. Volcker
Chairman, Board of Governors
Federal Reserve System
20th and Constitution, N.W.
Washington, D.C. 20551

Dear Paul:

I thought you might be interested in the enclosed letter and ad published by Equibank of Pittsburgh, Pennsylvania.

With best regards,

Sincerely,

Bill

WSM:plw

1979 OCT 29 PM 1:52

Equibank N.A.
Oliver Plaza
Pittsburgh, Pa. 15222

William E. Bierer
President

October 16, 1979

The Honorable William S. Moorhead
2207 Federal Building
Pittsburgh, Pennsylvania 15222

Dear Bill:

The inflation that has been eroding the foundation of our economy for more than a decade has recently led the Federal Reserve to tighten credit significantly. The Federal Reserve action will obviously require some sacrifices, but we think it was necessary in view of the threat that inflation poses to the whole economy.

Knowing you share our concern about inflation, I thought you would be interested in the enclosed ad describing our support of the Federal Reserve action. We are running this full-page public service ad in local newspapers to heighten the awareness of the general public about the dangers of inflation and the importance of replenishing the nation's capital base.

Sincerely,

Bill Bierer

Citation Information

Document Type: Advertisement

Number of Pages Removed: 2

Citations: Equibank. "Equibank Supports the Federal Reserve's Most Recent Decision in the Fight Against Inflation." October 1979.

October 30, 1979

The Honorable Lawton Chiles
Chairman
Subcommittee on Federal Spending
Practices and Open Government
Committee on Governmental Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Chiles:

Thank you for your letter of October 25 requesting the Board to testify at your Subcommittee's hearing on S. 1411, the Paperwork and Redtape Reduction Act of 1979.

I am pleased to inform you that Governor J. Charles Partee will appear on behalf of the Board on November 1 at 10:00 a.m.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-98)
bcc: Gov. Partee
Stan Sigel
Mrs. Mallardi (2)

ABRAHAM RIBICOFF, CONN., CHAIRMAN
HENRY M. JACKSON, WASH.
THOMAS F. EAGLETON, MO.
LAWTON CHILES, FLA.
SAM NUNN, GA.
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WILLIAM V. ROTH, JR., DEL.
TED STEVENS, ALASKA
CHARLES MC C. MATHIAS, JR., MD.
JOHN C. DANFORTH, MO.
WILLIAM S. COHEN, MAINE
DAVID DURENBERGER, MINN.

RICHARD A. WEGMAN
CHIEF COUNSEL AND STAFF DIRECTOR

Governor Partee will testify and r
is being prepared

RONALD A. CHIODO
CHIEF COUNSEL AND STAFF DIRECTOR

United States Senate

COMMITTEE ON
GOVERNMENTAL AFFAIRS
SUBCOMMITTEE ON FEDERAL SPENDING PRACTICES
AND OPEN GOVERNMENT
(202) 224-0211
WASHINGTON, D.C. 20510

#98

October 25, 1979

1979 OCT 29 PM 12:52

Mr. Paul A. Volcker
Chairman
Federal Reserve Board
20th and C Streets, N.W.
Washington, D.C. 20551

Dear Mr. Volcker:

The Senate Subcommittee on Federal Spending Practices and Open Government of the Committee on Governmental Affairs will hold a hearing on S. 1411, the Paperwork and Redtape Reduction Act of 1979, on Thursday, November 1, 1979. The bill strengthens and extends the reports clearance responsibilities of the Office of Management and Budget.

I would like to invite you or your representative to testify on this legislation. The hearing will begin at 10:00 a.m. and will be held in Room 3302 Dirksen Senate Office Building. It would be appreciated if you would deliver 50 copies of any prepared statement you might have to the Subcommittee Office by 5:00 p.m. the day before the hearing.

Should you have any questions regarding this hearing, Robert Coakley of the Subcommittee Staff, will be available to assist you. He may be reached at 224-0211 or in Room 44, 128 C Street, N.E. I look forward to hearing your testimony on this issue.

Sincerely

Lawton Chiles
LAWTON CHILES

BC: Mr. Jay Paul Brenneman
Congressional Liaison Office

October 30, 1979

The Honorable Norman E. D'Amours
House of Representatives
Washington, D. C. 20515

Dear Mr. D'Amours:

Thank you for your letter of October 24 concerning the invitation from Mr. DeWitt to speak before the New Hampshie Business and Industries Association. Because of a conflict in my schedule I will be unable to attend the New Hampshire meeting.

Sincerely,

S/Paul A. Volcker

cc: Mrs. Mallardi
#92

JRC:tjf

N M D'AMOURS
1 RICT, NEW HAMPSHIRE

STANDING COMMITTEES:
BANKING, FINANCE AND URBAN AFFAIRS
MERCHANT MARINE AND FISHERIES
MEMBER—STEERING AND POLICY COMMITTEE

Congress of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
1503 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-5456

DISTRICT OFFICES:
MANCHESTER, NEW HAMPSHIRE 03105
720 NORRIS COTTON FEDERAL BUILDING
275 CHESTNUT STREET
(603) 668-6800
669-7011, EXT. 526

PORTSMOUTH, NEW HAMPSHIRE 03801
425 AND 426 FEDERAL BUILDING
80 DANIEL STREET
(603) 436-7720, EXT. 707

LACONIA, NEW HAMPSHIRE 03246
200 AND 223 FEDERAL BUILDING
719 MAIN STREET
(603) 524-7185

192

October 24, 1979

Paul A. Volcker, Chairman
Federal Reserve Board
Federal Reserve Building
20th & Constitution Ave., N. W.
Washington, D. C. 20551

Dear Chairman Volcker:

I understand that Mr. Walter (Rink) DeWitt, President of the New Hampshire Business and Industries Association (BIA), has been in touch with Mr. Coyne of your office seeking your attendance on the evening of November 14th at the BIA's annual meeting in Bedford, New Hampshire.

The meeting will begin at 7:00 p. m. and your transportation to and from Bedford can very conveniently be arranged by the BIA since there is an airport within a few miles large enough to accommodate all classes of commercial and private airplanes. The BIA will be happy to arrange transportation to suit your schedule. It is estimated that 400 to 600 people will be in attendance.

I would like to ask you to please consider this as a personal request from myself that you attend the November 14th meeting if such is at all reconcilable with your busy schedule. I understand that Mr. DeWitt has been seeking to obtain a reply for the past few weeks. I have also spoken to Chairman Reuss of the House Banking Committee and he has asked me to inform you that he joins me in making this request and would be pleased to speak to you about it.

I would be most appreciative if you would arrange to have my office notified of whatever decision is reached in this matter prior to contacting Mr. DeWitt.

Thanking you for your anticipated cooperation, I remain,

Very truly yours,

Norm D'Amours

Norman E. D'Amours
Member of Congress

NED/sb
cc: Chairman Henry Reuss

October 30, 1979

The Honorable Henry S. Reuss
Chairman, Committee on Banking,
  Finance and Urban Affairs
House of Representatives
Washington, D. C. 20515

Dear Henry:

Thank you for your letter concerning an invitation to speak to the New Hampshire Business and Industries Association on November 14. Because of a conflicting commitment in Washington on that day I have been forced to regret the invitation.

Sincerely,

S/Paul A. Volcker

cc: Mrs. Mallardi
#93

JRC:tjf

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-SIXTH CONGRESS

2129 RAYBURN HOUSE OFFICE BUILDING

WASHINGTON, D.C. 20515

October 24, 1979

#93

Paul A. Volcker, Chairman
Federal Reserve Board
Federal Reserve Building
20th and Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Paul:

My colleague, Congressman Norman D'Amours, spoke to me about the request of the invitation which the New Hampshire Business and Industries Association has extended to you to speak to their annual meeting on November 14.

It would be greatly appreciated if your schedule could be arranged so that you could accept this invitation.

Sincerely,

Henry

Henry S. Reuss
Chairman

CC: Congressman Norman D'Amours

October 26, 1979

The Honorable Benjamin S. Rosenthal
Chairman
Commerce, Consumer, and Monetary
Affairs Subcommittee
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

As indicated in my letter of October 18, I am pleased to enclose the following information you requested:

(1) Copies of consumer complaints under the codes listed in your letter of August 20, 1979, handled by the New York Federal Reserve Bank during 1978 and the first two quarters of 1979 (to date, one complaint has not been located--we will forward it as soon as possible);

(2) A revised tabulation of the answers on the advertising page of the examination checklists for the last two examinations of state member banks in the State of New York;

(3) A tabulation of the answers on the advertising page of the examination checklists for the last two examinations of State member banks in the San Francisco district; and,

(4) A tabulation of the total number of advertising violations involving Regulation Q, the Fair Housing Act, and Regulation Z noted in examination reports for 1978 and the first two quarters of 1979 submitted by the New York and San Francisco Federal Reserve Banks.

Information regarding Washington, D.C., is not enclosed since we do not have a Reserve Bank in Washington, D.C. and have no direct compliance examination responsibilities with respect to any banks located in the District of Columbia.

I hope that the enclosed will complete the information requested. If, however, you or your staff have any questions, do not hesitate to call Jeanine Catalano, Review Examiner, at 452-3946.

Sincerely,

S/Paul A. Volcker

Enclosures

DJ:JC:smk (#V-46)
bcc: Diane Jeckins
Jeanine Catalano
Mrs. Mallardi(2)

October 18, 1979

The Honorable Benjamin S. Rosenthal
Chairman
Subcommittee on Commerce, Consumer
and Monetary Affairs
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Chairman Rosenthal:

As you requested in your letter of September 24, 1979, I am enclosing the following:

(1) Copies of consumer complaints under the codes listed in your letter of August 20, 1979, handled by the San Francisco Federal Reserve Bank during 1978 and the first two quarters of 1979.

(2) A tabulation of the answers on the advertising page of the examiner checklists for the last two examinations of State member banks in New York State.

To complete your request, I will forward the following information as soon as we can retrieve it:

(1) Copies of consumer complaints under the codes listed in your letter of August 20, 1979, handled by the New York Federal Reserve Bank during 1978 and the first two quarters of 1979.

(2) A tabulation of the answers on the advertising page of the examination checklists for the last two examinations of State member banks in the San Francisco district.

(3) A tabulation of the total number of advertising violations of Regulations Q and Z and the Fair Housing Act noted in the examination reports for 1978 and the first two quarters of 1979 submitted by the New York and San Francisco Federal Reserve Banks.

Members of the Board's staff and the staffs of these Reserve Banks are presently compiling this information. I will send it to you as soon as it is prepared.

If you or your staff have any questions, please feel free to contact Jeanine Catalano at 452-3946.

Sincerely,

S/Paul A. Volcker

JC:pjt (#V-46)
bcc: Jeanine Catalano
Mrs. Mallardi (2)

BENJAMIN S. ROSENTHAL, N.Y., CHAIRMAN
ROBERT T. MATSUI, CALIF.
EUGENE V. ATKINSON, PA.
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ELLIOTT H. LEVITAS, GA.

LYLE WILLIAMS, OHIO
JIM JEFFRIES, KANS.
JOEL DECKARD, IND.

MAJORITY—(202) 225-4407

NINETY-SIXTH CONGRESS

Congress of the United States

House of Representatives

COMMERCE, CONSUMER, AND MONETARY AFFAIRS SUBCOMMITTEE
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS

RAYBURN HOUSE OFFICE BUILDING, ROOM B-377
WASHINGTON, D.C. 20515

#46

September 24, 1979

BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
1979 SEP 25 PM 12:54
OFFICE OF THE CHAIRMAN

Hon. Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C. 20551

Dear Mr. Chairman:

In response to your letter dated September 7, 1979, and so that we can complete this hearing record on supervision of bank advertising practices, please send the subcommittee:

1. Actual complaints by the codes listed in our letter of August 20, 1979, for Reserve Banks in New York, San Francisco and Washington, D.C., for 1978 and the first two quarters of 1979.

2. The examination checklists for the last two examinations of State member banks in New York State, San Franciso and Washington, D.C.

3. A tabulation of the total number of violations in each region of Q1(a), Z9, and FHA 3 for 1978 and the first two quarters of 1979 for Reserve Banks in New York, San Francisco and Washington, D.C.

We request a letter for our hearing record as soon as possible with a timetable for receiving these documents from you. After evaluating the documents, the subcommittee may request additional information to complete the record.

Thank you for your time and consideration.

Sincerely,

Benjamin S. Rosenthal
Chairman

BSR:tb

Actio[n] assigned to Janet Hart

October 26, 1979

The Honorable Paul E. Tsongas
Chairman
Consumer Affairs Subcommittee
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

In your letter of October 4, 1979, you requested information concerning the Regulation Z interagency enforcement guidelines and the requirement that banks within our supervisory jurisdiction conduct file searches to identify reimbursable violations.

Your initial request is for: (a) the number of file searches ordered by this agency; (b) the specific complaints; (c) the steps taken by our staff to verify the cost factors claimed by the institutions; and (d) whether the file searches were, in fact, conducted in accordance with the instructions supplied by our agency.

Generally, our examiners do not request a bank to conduct a file search unless a pattern or practice of reimbursable violations is manifest in the examiner's loan sample. Even when a file search must be initiated, it is usually limited to that type of loan in the bank's portfolio that has been found to contain the pattern or practice. Through July 1979, the Reserve Banks have asked 387 banks out of 523 with reimbursable violations to undertake file searches. The banks are required to report the results of the file searches to the Reserve Banks which review the results for reasonableness based on the reported data. The Reserve Banks review the results of the file searches on a sample basis during the next examination to determine the extent to which the banks have reviewed their files and the adequacy of the calculated reimbursement amounts.

The Board and the Reserve Banks have received very few specific complaints from banks objecting to the file searches. Those complaints that do mention file searches focus on the contention that it costs the bank more to conduct the file search than to reimburse, but no specific data has been supplied. This is one of the factors that led the Board, and the other agencies on the Federal Financial Institutions Examination Council, to ask for information on the direct and indirect costs of implementing the guidelines in the recent proposal to amend the guidelines, and for comment on ways in which the guidelines could be amended to reduce administrative burdens on financial institutions while maintaining fairness to the consumer. A copy of that proposal, with a press release dated October 15, is enclosed.

You also ask for our response to a statement made by Mr. John H. Perkins, President of the American Bankers Association in a letter to its members on August 21, 1979. Apparently, Mr. Perkins contends that bankers have made a conscientious effort to comply with Regulation Z, that violations were cited despite the bankers' good faith efforts to comply with their understanding of the law's requirements at the time the loans were made, but that the agencies, in implementing the guidelines, retroactively apply changed interpretations and amendments to loan transactions. In our response you ask for: (1) a listing of the major reimbursable violations (in the order of their magnitude) cited by this agency along with the number of banks cited for that type of violation; and (2) a statement of how the rules and interpretations relating to each practice may have been altered since 1974.

As the Board has stated previously, in Annual Reports to Congress and elsewhere, we believe that most bankers have indeed made a conscientious effort to comply with the law. We believe that most of the violations discovered have been technical in nature and have occurred because the bank misunderstood the law's requirements rather than because it made a conscious effort to violate the law.

In response to Mr. Perkins' assertions regarding retroactive application of changed interpretations and amendments, and in response to item (2) of your request, we offer the following. The Board's staff has been concerned about this issue but has been unable to find an instance in which a change in the law imposing more stringent compliance requirements has been enforced with respect to pre-existing transactions. It would not be the Board's policy to enforce new, more stringent requirements retroactively.

There have, of course, been changes in Regulation Z since 1974. It is our belief, however, that most of the interpretations of and changes in Regulation Z have come in response to legislative change or to requests for clarifications of the law's requirements that were submitted by creditors. In a substantial portion of those latter instances, the interpretation or amendment served to clarify the law's requirements at the time rather than changing those requirements. We believe that in those cases where a substantive change was made, particularly with regard to requirements relating to the reimbursement policies, the effect of the change was to ease necessary compliance, rather than making compliance more stringent. For example, the "minor irregularities" provision of the regulation was amended to simplify the annual percentage rate calculation for certain loans with irregular first payment periods. In addition, the staff issued an official interpretation clarifying that disclosures necessary to exclude credit life insurance premiums from the finance charge can be made separately from the other required disclosures. We believe that both of these interpretations had the effect of simplifying, rather than increasing, the creditors' compliance effort. We would, of course, wish to be informed of any examples Mr. Perkins may have of the types of actions he addressed.

Enclosed is a tabulation that responds to (1), above. This tabulation breaks down the major categories of reimbursable violations and ranks each violation within the category by its relative frequency. The number of banks having the type of violation indicated by the general categories is also provided. The figures are based on the 523 banks that had reimbursable violations as of July 31, 1979, and covers the period from March 1977 through July 1979.

I hope this information is of assistance to you.

Sincerely,

S/Paul A. Volcker

Enclosures
TRB:smk (#V-64)
bcc: Mr. Burniston
Mrs. Mallardi(2)

Number of Banks with Reimbursable Violations By General Category*

Category	Number of Banks
1. Understated APR	368
a) failure to correctly treat prepaid finance charges (e.g., points) in APR.	
b) failure to include origination and service fees in APR calculation.	
c) misapplication of the "minor irregularities" provisions.	
d) disclosures based on 360/360 or 365/365 basis but customer charged on 365/360 basis.	
e) failure to disclose the APR.	
f) misunderstanding of the rounding provisions.	
2. Understated Finance Charge	155
a) failure to correctly treat prepaid finance charges in finance charge disclosure.	
b) failure to include origination and service fees in finance charge disclosure.	
c) failure to include mortgage guaranty insurance in the finance charge.	
3. Credit Life Violations	70
a) failure to include the cost of credit life insurance in the finance charge when the optional nature is not disclosed.	
b) failure to obtain the customer's signature or disclose the cost of optional insurance.	
4. Non-Finance Charge Violations	2
a) disclosing actuarial method of rebating unearned finance charges but using Rule of 78's.	

* Based on 523 banks found to have reimbursable violations between March 1977 - Ju[illegible] 79.

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, D.C. 20510

October 4, 1979

#64

The Honorable Paul A. Volcker
Chairman
Board of Governors of the
Federal Reserve System
Washington, D.C. 20037

Dear Chairman,

Recently there has been a considerable amount of discussion concerning the requirement by various Federal Financial Regulatory Agencies, under the uniform enforcement guidelines for Truth-In-Lending, that financial institutions perform file searches to locate reimbursable violations of Truth-In-Lending.

It is my understanding that the Federal Reserve Board has received complaints from institutions under its supervision which have conducted file searches under the uniform guidelines. It would be helpful to our understanding of this issue if your staff could document the cases that have been brought to their attention.

It would be particularly helpful if you would forward a statement setting forth: a.) the number of file searches ordered by your agency, b.) the specific complaints, c.) what steps have been taken by your staff to verify the cost factors claimed by the institutions, and d.) whether the file searches were, in fact, conducted in accordance with the instructions supplied by your agency.

I would also appreciate your response to the following statement by John H. Perkins, President of the American Bankers Association in a letter to members of the association dated August 21, 1979:

> "The point that must come first in any discussion of Truth-In-Lending enforcement is this: bankers have conscientiously tried to comply with the regulations. Virtually all of the so-called violations in fact represented good faith compliance in past years with the rules which applied at that time. As we all know, the rules and interpretations have changed constantly and are continuing to change, yet we are being judged on past practices on the basis of new interpretations which did not even exist at the time of the transactions."

Would you please include in your response: a.) a listing of the major reimbursable violations (in the order of their magnitude) cited by your agency along with the number of banks cited for that type of violation, and b.) a statement of how the rules and interpretations relating to each practice may have been altered since 1974.

In order to be of assistance, it would be appreciated if this response could be forwarded by October 15.

Best wishes,

Sincerely,

Paul Tsongas

Paul E. Tsongas, Chairman
Consumer Affairs Subcommittee

October 25, 1979

The Honorable Harrison A. Williams, Jr.
United States Senate
Washington, D. C. 20510

Dear Senator Williams:

Thank you for your letter of October 18 recommending Ms. Marilyn E. Schoeck as a member of the Board's Consumer Advisory Council.

You may be assured that Ms. Schoeck's qualifications will receive full consideration by the Board when it makes the 1980 appointments to the Council within the next several weeks. We will be in touch with you when the selections are made.

The Board appreciates receiving your recommendation and your interest in the Consumer Advisory Council.

Sincerely,

S/Paul A. Volcker

CO:vcd (#V-87)

IDENTICAL LETTER TO CONG. MILLICENT FENWICK (#V-90)

bcc: Mrs. Mallardi (2)
Anne Geary (w/copies of incoming ltrs.)

WILLIAM PROXMIRE, WIS., CHAIRMAN

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MARY FRANCES DE LA PAVA, CHIEF CLERK

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, D.C. 20510

October 18, 1979

1979 OCT 22 AM 9:06

#87

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C. 20551

Dear Chairman Volcker:

Ms. Marilyn E. Schoeck of Milburn, New Jersey has been recommended to the Federal Reserve Board to serve as a member of the Consumer Advisory Council. The purpose of this letter is to endorse her nomination and urge her appointment.

I have met with Ms. Schoeck to discuss both her interest in the Consumer Advisory Council as well as the contribution she could make to its work. I am impressed that she can bring very necessary perspectives to the Council as a result of her work in New Jersey's second largest bank holding company.

Many of the laws passed by the Congress in recent years have been oriented toward the protection of the consumer in an increasingly technologically-oriented financial marketplace. Ms. Schoeck's experience would be most useful because of her work with the various kinds of funds transfer devices now being employed and deployed by financial institutions. She has first-hand familiarity with the technical and business aspects of serving consumer needs using technology. Moreover, she has been actively coordinating her institutions compliance with all the requirements imposed by the Congress and the regulators to protect consumers.

For the work of the Consumer Advisory Council to be useful to the Federal Reserve Board, it is essential to attract the advice of individuals who are knowledgeable about the capabilities of new electronic consumer products and who are sensitive to the needs of consumers. Ms. Schoeck has been actively performing this function for her employer and for the benefit of the New Jersey Bankers' Association, the Electronic Fund Transfer Association and other professional associations.

I urge you to consider her credentials carefully and trust you will be equally impressed. Ms. Schoeck would be an excellent appointment for you to make to the Consumer Advisory Council.

Sincerely,

Harrison A. Williams, Jr.

cc. Ms. Anne Geary

October 25, 1979

The Honorable Bill Chappell
Member of Congress
[redacted]

Dear Mr. Chappell:

I am pleased to respond to your letter of October 17 regarding a request from your constituent, Mr. Lloyd A. Childress, for information on the Federal Reserve System.

The Federal Reserve System--the nation's central bank--was created by Act of Congress on December 23, 1913. The System has a pyramidal structure: at its base are about 5,600 member commercial banks; in the middle is a nationwide network of 12 Federal Reserve Banks and 25 branches; and, at the apex of the organization, is a seven-member Board of Governors, with headquarters in Washington, D.C.

As provided for by law, the stock of the Federal Reserve Banks is held entirely by commercial banks that are members of the Federal Reserve System. However, ownership of that stock is in the nature of an obligation incident to membership and does not carry with it the attributes of control and financial interest ordinarily attached to stock ownership in corporations that are operated for the purpose of making a profit. The amount of stock that member banks are required to own is specified by law. The stock may not be sold or pledged as security for loans, and dividends are limited by law to six per cent per annum.

The Federal Reserve Banks are not operated for a profit. Each year, in fact, they turn over substantial sums of money directly to the U.S. Treasury. As a result of earnings in 1978, payments to the U.S. Treasury amounted to over $7 billion, as indicated in the enclosed press release.

To provide further background on the Federal Reserve System, I am enclosing a booklet entitled "The Federal Reserve System--Purposes and Functions." In addition, enclosed is a copy of the 1978 Annual Report of the Board of Governors. Beginning on page 383 is the financial statement for the Board, followed by detailed statement of condition tables of the Federal Reserve Banks for the year 1978.

I hope this information will be useful to Mr. Childress. Please let me know if I can be of further assistance.

Sincerely yours,

(Signed) Donald J. Winn

Donald J. Winn
Special Asst. to the Board

CO:pjt (#V-88)
bcc: Mrs. Mallardi

Enclosures

BILL CHAPPELL
4TH DISTRICT, FLORIDA

2353 RAYBURN OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-4035

COMMITTEE:
APPROPRIATIONS

SUBCOMMITTEES:
DEFENSE
ENERGY AND WATER DEVELOPMENT
DISTRICT OF COLUMBIA

Congress of the United States
House of Representatives
Washington, D.C. 20515

DISTRICT OFFICES:
258 FEDERAL BUILDING
OCALA, FLORIDA 32670
(904) 629-0039

523 NORTH HALIFAX
DAYTONA BEACH, FLORIDA 32018
(904) 253-7632

8829 SAN JOSE BOULEVARD
JACKSONVILLE, FLORIDA 32217
(904) 733-4288

October 17, 1979

#88

1979 OCT 22 PM 3:05

Mr. Paul A. Volcker, Chairman
Board of Governors of the Federal Reserve System
Federal Reserve Building
Constitution Avenue Between 20th & 21st Sts.
Washington, D. C. 20551

Re: Federal Reserve System - Information-Lloyd A. Childress

Dear Mr. Volcker:

The attached communication is sent for your consideration. It will be appreciated if you will please investigate the statements contained therein and forward me the necessary information for reply, returning the enclosed correspondence with your answer.

With best wishes, I am

Sincerely,

Bill Chappell

BILL CHAPPELL
Congressman

BC:rks
encl.

PLEASE RESPOND TO:

☐ WASHINGTON ☐ OCALA ☑ DAYTONA BEACH ☐ JACKSONVILLE

REGISTERED REAL ESTATE BROKER

STROUT REALTY, Inc.

ROUTE 92, EAST; ROUTE 5, BOX 1201
DE LAND, FLORIDA 32720
PHONE: (904) 734-7775

LLOYD A. CHILDRESS
Associate

October 10, 1979

The Honorable Bill Chappell, Jr.
[redacted]

Dear Congressman Chappell:

I am very interested in the Federal Reserve System and would like to receive the following:

- Copy of the operating statement
- Structure of the System
- Who owns the Federal Reserve Banks
- The disposition of the profits of the Federal Reserve System

An early reply will be most appreciated. Thank you.

Yours truly,

Lloyd A. Childress

LAC:fl

October 25, 1979

The Honorable S. William Green
House of Representatives
Washington, D. C. 20515

Dear Mr. Green:

Thank you for your letter of October 17 indicating your support for the establishment of International Banking Facilities within the continental United States.

The Board last considered this proposal at its meeting of July 16, 1979, and decided to take no formal action at this time. The Board found that several of the significant policy and legal issues raised by public comments and by the Board's staff appeared to be related inextricably to anticipated legislative and administrative initiatives. Some of these issues relate to monetary control, competitive advantages enjoyed by banks located in New York, and legal aspects of implementing the proposal. The Board requested its staff to continue work on the substantive issues raised by the proposal and to provide a report in about six months.

I shall be glad to keep you informed of further developments in this matter.

Sincerely,

S/Paul A. Volcker

RFG:vcd (#V-85)

bcc: Mrs. Mallardi (2)
Messrs. Gemmill, Schwartz, Simpson
Ms. Brown
Mr. Truman (for Division Files)

S. WILLIAM GREEN
18TH DISTRICT, NEW YORK

COMMITTEES:
BANKING, FINANCE AND URBAN AFFAIRS

SUBCOMMITTEES:
HOUSING AND COMMUNITY DEVELOPMENT
ECONOMIC STABILIZATION
GENERAL OVERSIGHT AND RENEGOTIATION

SELECT COMMITTEE ON AGING

Congress of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
1118 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-2436

NEW YORK OFFICES:
1628 SECOND AVENUE (84TH STREET)
NEW YORK, NEW YORK 10028
(212) 826-4466

229 FIRST AVENUE (14TH STREET)
NEW YORK, NEW YORK 10003
(212) 826-4466

October 17, 1979

#85

The Honorable Paul A. Volcker
Chairman
Board of Governors of the Federal Reserve System
Washington, D. C. 20551

Dear Chairman Volcker:

As a Member of Congress from New York City who serves on the House Banking, Finance and Urban Affairs Committee, I urge your support of the proposal to permit the establishment of International Banking Facilities--or "free trade zones"--within the continental United States. These Facilities, of course, would operate under reserve and interest rate provisions that would allow them to be fully competitive with international banking in foreign cities.

As a past President of the New York Federal Reserve, you are, I know, familiar with this issue and understand the need to keep U.S. financial centers, particularly New York City, competitive with the other financial centers of the world. The competitive position in the U.S. of the U.S. banks has declined in the past ten years, and the "free trade zone" proposal would tend to reverse this alarming competitive deterioration. This would have many advantages for the United States. First, of course, a restoration of U.S. financial center primacy should give the Fed greater ability to work toward orderly economic growth and change. Second, the direct economic benefits could be considerable. If the recent financial sector job growth in London is any indication, the potential for job growth in the U.S. is impressive--especially for New York City.

While New York stands to gain from implementation of this proposal, other states will also gain. The proposal is not limited to New York. In addition to setting up IBF's elsewhere, banks in other cities would be able to participate in the New York IBF through such vehicles as Edge Act corporation subsidiaries.

I will not try to cover all of the points which are being argued in support of the International Banking Facility proposal. Suffice it to say, I am convinced that favorable action by the Board of Governors would be in the best interests of the United States and of New York. Accordingly, I respectfully urge that you permit the establishment of International Banking Facilities, as proposed on a basis which would permit them to compete with their overseas counterparts.

I await with interest decision of the Board on this most important matter. Thank you for your courtesy and concern.

Sincerely,

Bill Green

S. William Green
Member of Congress

SWG:nhd

October 25, 1979

The Honorable Stanley N. Lundine
House of Representatives
Washington, D. C. 20515

Dear Mr. Lundine:

Thank you for your recent letter concerning the bankers convention in Olean, New York, on November 13.

We have arranged for Ron Gray, Senior Vice President of the Federal Reserve Bank of New York, to meet with the group in Olean on that date. Mr. Gray is familiar with western New York, having once been the head of our Buffalo Branch, and I am sure that the bankers will find his remarks informative.

With best regards.

Sincerely,

S/Paul A. Volcker

cc: Mrs. Mallardi
#77

JRC:tjf

JRC

STANLEY N. LUNDINE
39TH DISTRICT, NEW YORK

COMMITTEE ON
BANKING, FINANCE AND
URBAN AFFAIRS

COMMITTEE ON
SCIENCE AND TECHNOLOGY

SELECT COMMITTEE ON
AGING

430 CANNON BUILDING
WASHINGTON, D.C. 20515
PHONE: 202-225-3161

Congress of the United States
House of Representatives
Washington, D.C. 20515

DISTRICT OFFICES:

ROOM 122, FEDERAL BUILDING
P.O. BOX 908
JAMESTOWN, NEW YORK 14701
PHONE: 716-484-0252

180 STATE STREET
ELMIRA, NEW YORK 14901
PHONE: 607-734-0302

ROOM 606, 101 N. UNION STREET
OLEAN, NEW YORK 14760
PHONE: 716-372-1818

#77

1979 OCT 15 PM 1:01

Friday, October 12, 1979

Paul A. Volcker
Chairman
Federal Reserve Board
20th and C Streets, N.W.
Washington, D.C. 20551

Dear Mr. Volcker:

My Olean district office has contacted the Federal Reserve Board to request a speaker for a banker's convention to be held in my Western New York district, and Jay Brenneman, of your office, has advised my office to forward that request in writing.

I am requesting that the Federal Reserve Board provide a personable and knowledgeable speaker to the banker's meeting, scheduled for Tuesday, November 13, at the Castle Restaurant in Olean, New York. A brief, thirty-minute talk about a timely, interesting topic of your choice, followed by a few minutes of questions and answers, would be very welcome to the more than 100 bankers and guests attending the function.

I would ask that you provide my Olean district office manager, Elisabeth Johnson, with the name of your speaker and a copy of his curriculum vitae as soon as possible, so that she may publicize the evening event. She will also be pleased to provide you with travel information, and the bankers, of course, will provide an escort for the event. Her FTS telephone number is 432-4232.

Thank you for your assistance in this matter. Please do not hesitate to contact my office at any time, if I may be of further assistance to you in this or other matters.

Sincerely,

Stan

Stanley N. Lundine
Member of Congress

October 25, 1979

The Honorable Stephen L. Neal
Chairman
Subcommittee on International Trade,
Investment and Monetary Policy
Committee on Banking, Finance and
Urban Affairs
House of Representatives
Washington, D.C. 20515

The Honorable Parren J. Mitchell
Chairman
Subcommittee on Domestic Monetary Policy
Committee on Banking, Finance and
Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Chairmen Neal and Mitchell:

Thank you for your recent invitation to appear before your Subcommittees at oversight hearings on "Monetary Policy--Goals and Conduct for the 1980's."

I am looking forward to appearing at this joint hearing on November 13 at 9:30 a.m.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-66)
bcc: Mr. Axilrod
Mrs. Mallardi (2)

October 24, 1979

The Honorable John Heinz
United States Senate
Washington, D.C. 20510

Dear Senator Heinz:

In reply to your letter of October 15, I am pleased to enclose a copy of the Board's views on S. 1592 as submitted to the Senate Committee on Banking, Housing and Urban Affairs.

Sincerely,

S/Paul A. Volcker

Enclosure

CRM:pjt (#V-81)
bcc: Mr. McNeill
Mrs. Mallardi (2)

October 24, 1979

The Honorable William Proxmire
Chairman
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Proxmire:

This is in reply to your request for comment on S. 1592, the proposed "Financial Regulation Simplification Act of 1979."

The Board has consistently expressed its support of the general policy and goals of S. 1592. In fact, as you know, the Board has adopted regulatory procedures that generally conform to the bill's proposals.

However, in adopting these procedures, the Board found that certain exceptions were necessary. Monetary policy regulations often do not fit into such a general procedural framework because the public interest sometimes requires such actions to be taken swiftly and without prior public knowledge. We also concluded that the general procedures need not be applied to another group of regulations where compliance with such procedures would be impracticable, unnecessary or contrary to the public interest. For example, an extended comment period and extensive consideration of alternatives may not be either possible or desirable in the case of (1) technical or clarifying amendments, (2) regulations designed to eliminate a loophole or reduce a burden where further delay would cause unnecessary harm, (3) regulations that would reformulate a proposal previously issued for public comment, or (4) regulations subject to a short statutory deadline.

It is recommended that S. 1592 be amended to recognize the need for such variations from the general policy outlined in the bill. The Board will be happy to cooperate with you and your Committee in efforts to achieve a less burdensome regulatory environment.

Sincerely,

S/Paul A. Volcker

plus (V-81)
CRM:pjt/(per request for comments on bill)
bcc: Mr. McNeill
Mrs. Mallardi (2)

Action assigned to Neil Petersen
and Charlie McNeill

United States Senate
COMMITTEE ON FINANCE
WASHINGTON, D.C. 20510

#181

1979 OCT 18 AM 9:43

October 15, 1979

Mr. Paul Volcker, Chairman
Federal Reserve Board of Governors
Constitution Avenue and
20th Street, NW
Washington, DC

Dear Mr. Chairman:

On July 27, 1979, I introduced, along with Senators Dole and Lugar, S.1592, the Financial Regulation Simplification Act of 1979. The bill is designed to assure the elimination of duplicative or conflicting regulations, and that regulations are clearly and simply expressed, and that duplicative and conflicting regulations are eliminated or clarified.

On August 3, 1979, the Banking Committee officially requested comments by the Federal Reserve Board on this legislation. Thus far, there has been no response.

I would, therefore, appreciate any efforts that can be made to provide the Committee with comments in the near future. Thank you for your consideration of this matter.

Sincerely,

John Heinz

John Heinz
United States Senate

JH/hsr

JESSE HELMS
NORTH CAROLINA

United States Senate

WASHINGTON, D.C. 20510

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

1979 OCT 16 AM 11: 18

RECEIVED
OFFICE OF THE CHAIRMAN

October 15, 1979

Have Rex arrange a breakfast

224-6342

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Constitution Avenue
Washington, D.C. 20551

Called 10/18 ew

Dear Mr. Chairman:

I have been remiss in not responding far earlier to your thoughtful note of September 19. I apologize for the delay.

I would be honored to meet with you at your convenience. Also, I would like for you to meet a splendid young associate of mine, Howard Segermark, who is very knowledgeable on the issues of mutual interest to you and me. If he could sit in with us, it would be most helpful to me.

Let me commend you on the courageous positions you have taken. Nobody likes to dish out unpopular medicine, but the country's ailment demands that we do what is right though it may be unpopular at the moment.

Sincerely,

Jesse Helms

JESSE HELMS:pd

11/15 @ 815 am

WARREN J. MITCHELL, MD., CHAIRMAN
STEPHEN L. NEAL, N.C.
NORMAN E. D'AMOURS, N.H.
DOUG BARNARD, GA.
JIM MATTOX, TEX.
JOHN J. CAVANAUGH, NEBR.

225-7315

GEORGE HANSEN IDAHO
RON PAUL, TEX.
DON RITTER, PA.

U.S. HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON DOMESTIC MONETARY POLICY
OF THE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SIXTH CONGRESS
WASHINGTON, D.C. 20515

October 9, 1979

The Honorable Paul A. Volcker
Chairman, Board of Governors
Federal Reserve System
20th and Constitution Avenue N.W.
Washington, D.C. 20551

Dear Mr. Chairman:

On November 13, 14 and 15, the Subcommittee on Domestic Monetary Policy and the Subcommittee on International Trade, Investment and Monetary Policy will hold joint oversight hearings on "Monetary Policy -- Goals and Conduct for the 1980's." We would appreciate hearing your views on this subject and invite you to testify on November 13 at 9:30 a.m. in Room 2128 Rayburn House Office Building.

Although we do not want to limit your testimony in any way, we would like to hear your assessment of the merits of two alternative monetary policy strategies for the 1980's.

Strategy 1 places top priority on halting the decline in the value of the dollar on the foreign exchange markets, and proposes to do so by keeping money "tight" at home and resisting speculative attacks against the dollar abroad until the decline is halted. Under this strategy, in the months immediately ahead, the Federal Reserve would raise the Federal funds rate substantially above the current level. The purpose would be to raise U.S. short term interest rates and slow U.S. money growth so as to provide incentives for money managers around the world to buy dollars and hold dollar denominated securities. Simultaneously, the Federal Reserve and the Treasury would intervene vigorously on the foreign exchange markets, in cooperation with other central banks, to combat any excessive fluctuations in exchange rates that might arise from speculation against the dollar even in the face of high interest rates. After the dollar had been stabilized, primarily against the German mark, sufficiently long to convince foreign exchange traders that further precipitous declines would not be tolerated, monetary policy could be gradually re-oriented toward the domestic goals of full employment and price level stability.

What risks would this strategy entail? Can such a policy succeed without the cooperation of foreign central banks? That is, would our raising interest rates not invite retaliation by foreign central banks, and hence a spiraling upward of interest rates worldwide without noticeable effect on the foreign exchange value of the dollar? Even assuming a policy of cooperation by foreign central banks, would not maintaining the funds rate at a higher level than currently prevails precipitate a sharp deceleration of money growth and consequent recession? Would not fighting that recession, and even the expectation of fighting it, again destabilize exchange rate markets?

Strategy 2 would ignore movements in interest rates and concentrate instead on establishing and remaining on or near a long run disinflationary monetary growth target path. (See, for example, the letter to you dated September 5, signed by seven members of the Domestic Monetary Policy Subcommittee, and H.R. 5476, recently introduced by Mr. Neal. For your convenience, these documents are enclosed.)

Can this strategy be followed independently of the monetary policies pursued by other central banks? Would it help to promote achievement of the 1983 Hawkins-Humphrey Act goals of 4 percent unemployment and 3 percent inflation and at the same time to stabilize the value of the dollar on foreign exchange markets? What risks does it involve? Should it be adhered to in the face of increases in interest rates and unemployment? If the strategy is not binding, how can we convince investors and traders around the world that we are serious about reducing inflation and that the exchange rate risk from holding dollar denominated assets will diminish?

Further in this regard, is there reason to believe that adhering to an announced long run disinflationary monetary growth target path would lead to higher interest rates and higher unemployment than would a policy that accelerated money growth when interest rates and unemployment moved higher? Would it not be wiser to hold fast to the announced monetary growth target path even in the face of temporary increases in unemployment, which could be dealt with by pinpointed fiscal policies?

Finally, we note that recently the Federal Reserve raised its discount rate from 11 to 12 percent and at the same time announced that the Open Market Committee will try to control monetary growth by metering the flow of reserves instead of manipulating the Federal funds rate. The discount rate rise would appear consistent with Strategy 1 while the change in operating procedure seems consistent with Strategy 2. We would appreciate your comments on the meanings of these recent changes in policy and tactics by the Federal Reserve.

We look forward to hearing your views on these and other questions you may want to address on November 13.

Sincerely,

Steve Neal

Stephen L. Neal, M.C.
Chairman, Subcommittee on
International Trade, Investment
and Monetary Policy

Parren J. Mitchell

Parren J. Mitchell, M.C.
Chairman, Subcommittee on
Domestic Monetary Policy

PJMSLN/rwt
enclosures

October 24, 1979

The Honorable Lee H. Hamilton
House of Representatives
Washington, D.C. 20515

Dear Mr. Hamilton:

I am pleased to respond to your recent letter regarding Henry Kaufman's criticism of Federal Reserve policy. Mr. Kaufman argues that the Fed has focused its attention too narrowly on the monetary aggregates--particularly M-1--and that a broad credit aggregate would provide a better guide for policy.

System economists have examined this argument recently. Earlier this year while I was still at the New York Bank, a senior official, Richard Davis, published an article in our quarterly economic review on this subject. More recently, a memorandum prepared by the Board staff was sent to Senator Proxmire in response to his request for an analysis of Mr. Kaufman's argument. I am enclosing copies of these two pieces for your examination.

In brief, we believe that there is much to be said for monitoring credit flows, since they reflect the transmission of monetary policy to the economy. The Board and the Federal Open Market Committee do examine credit developments in some detail; indeed, the data Mr. Kaufman employs are produced by the Board of Governors. The issue is whether some broad credit aggregate would be a better intermediate target for monetary policy, and on this we have serious doubts. High correlation of time series is not a sufficient condition for a good target; such considerations as lead-lag relationships, timeliness and quality of data, and controllability are critical. As is indicated in the staff memorandum, credit aggregates appear deficient on these scores.

The Federal Reserve will continue to give careful attention to the cost and volume of credit as it assesses its policies, and our staff will continue to investigate the relationships among monetary growth, credit flows, and the performance of the economy. At the present time, however, it would appear unwise to subordinate monetary aggregates to credit aggregates as intermediate targets for policy.

Sincerely,

S/Paul A. Volcker

MJP:SHA:JPB:pjt (#V-73)
bcc: Messrs. Axilrod & Prell
Mrs. Mallardi (2)

Enclosures ("[illegible]"

LEE H. HAMILTON
9TH DISTRICT, INDIANA

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October 11, 1979

#73

Honorable Paul A. Volcker, Chairman
Board of Governors of the Federal
Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

It was with great interest that I read Mr. Henry Kaufman's article, "Where The Fed Has Gone Awry," in the October 7 edition of The New York Times. The article contains a very basic criticism of current monetary policy. The criticism is, I think, one which must be addressed squarely.

The gist of Mr. Kaufman's critical view can be captured in a few of the article's passages. To begin, Mr. Kaufman notes that the "issue is whether the Federal Reserve Board, by focusing for the last five years upon a very narrow statistical concept called the M-1 money supply, is using a monetary policy target that is relevant to today's economic and monetary reality." Mr. Kaufman himself takes sides on the issue a bit later when he says that the "failure of monetary policy lies in the Federal Reserve limiting its target to the narrow statistical concept of the money supply." Finally, Mr. Kaufman proceeds to tie the "failure of monetary policy" to our economic problems in a predictable way, remarking that the "real story behind our severely aggravated inflation is that the growth of credit has been proliferating while the Federal Reserve has been focusing on the M-1 and M-2 money supplies."

Inflation is the most serious problem on the nation's domestic agenda. Consequently, the policies of government must be justified in detail if they are alleged to contribute to inflation in a significant manner. I would deeply appreciate your response to the criticism outlined above. A copy of Mr. Kaufman's article is enclosed for your convenience. I look forward to hearing from you at the earliest possible date.

With best wishes, I am

Sincerely yours,

Lee H Hamilton

LEE H. HAMILTON, M.C.

LHH:vbm
enclosure

Where the Fed Has Gone Awry

By HENRY KAUFMAN

IT is incredible that there has been virtually no general public discussion or debate in financial circles so far this year over the targets for monetary policy that the Federal Reserve has employed in its attempts to foster orderly economic growth. Something, after all, has gone wrong in the monetary mechanism. Our economy is being buffeted by high rates of inflation and is engulfed by deep-rooted fears of future economic instability.

The Federal Reserve itself has recognized some of the problems in the monetary targets it is now using and, in fact, earlier this year said it would try to improve their quality and effectiveness. Public comment was invited, but the discussion so far has been remarkably subdued, even though the future credibility and technical efficiency of United States monetary policy are at stake.

Despite the apparent technicality of the issue, what is involved can affect every economic participant in the country. The inflation rate of 11.5 percent for the past 12 months, as measured by the Consumer Price Index, could double our price level again in the next six years — that is, by 1985 — if it is not brought down. Prices have already doubled since 1969, with most of the increase in the years since 1975. Yet, there is no concrete assurance that we will experience anything more than temporary relief from inflation because the nation has not reached that point where the citizenry faces the sacrifices that may be unavoidable if inflation is to be reduced substantially. On the contrary, more and more economic and financial decisions are being made by Americans and foreigners who do business with us on the assumption that inflation is going to continue unabated. The historical record is very clear that this only intensifies inflation and heightens the flight from money into the materiality of land, goods and precious metals.

What is at issue is whether the Federal Reserve Board, by focusing for the last five years upon a very narrow

POINT OF VIEW

statistical concept called the M-1 money supply, is using a monetary policy target that is relevant to today's economic and monetary reality. The M-1 money supply consists of demand deposits plus cash in circulation.

The existing approach of the Federal Reserve, which was formally adopted in 1974, depends upon the presumed linkages between interest-rate levels, changes in the supply of money that are generally implicit in changes in banking reserves, and economic activity.

The assumed cause and effect sequence generally goes as follows: Changes in banking reserves and resultant changes in the market's key interest rate (the Federal funds rate) together will influence changes in the money supply which, in turn, will affect economic activity. This unalloyed monetarism is not materially changed by the newer "practical monetarism," which holds that the relationship be-

Continued on Page 14

›ther Way to Count the Money Supply

Page 1
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›. They cite an overly
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›owth Targets
›vth Rate

›rget (%)	Rate (%)
›½–7½	5.8
›½–6½	7.9
4–6½	7.2
›½–4½	4.5*

›9

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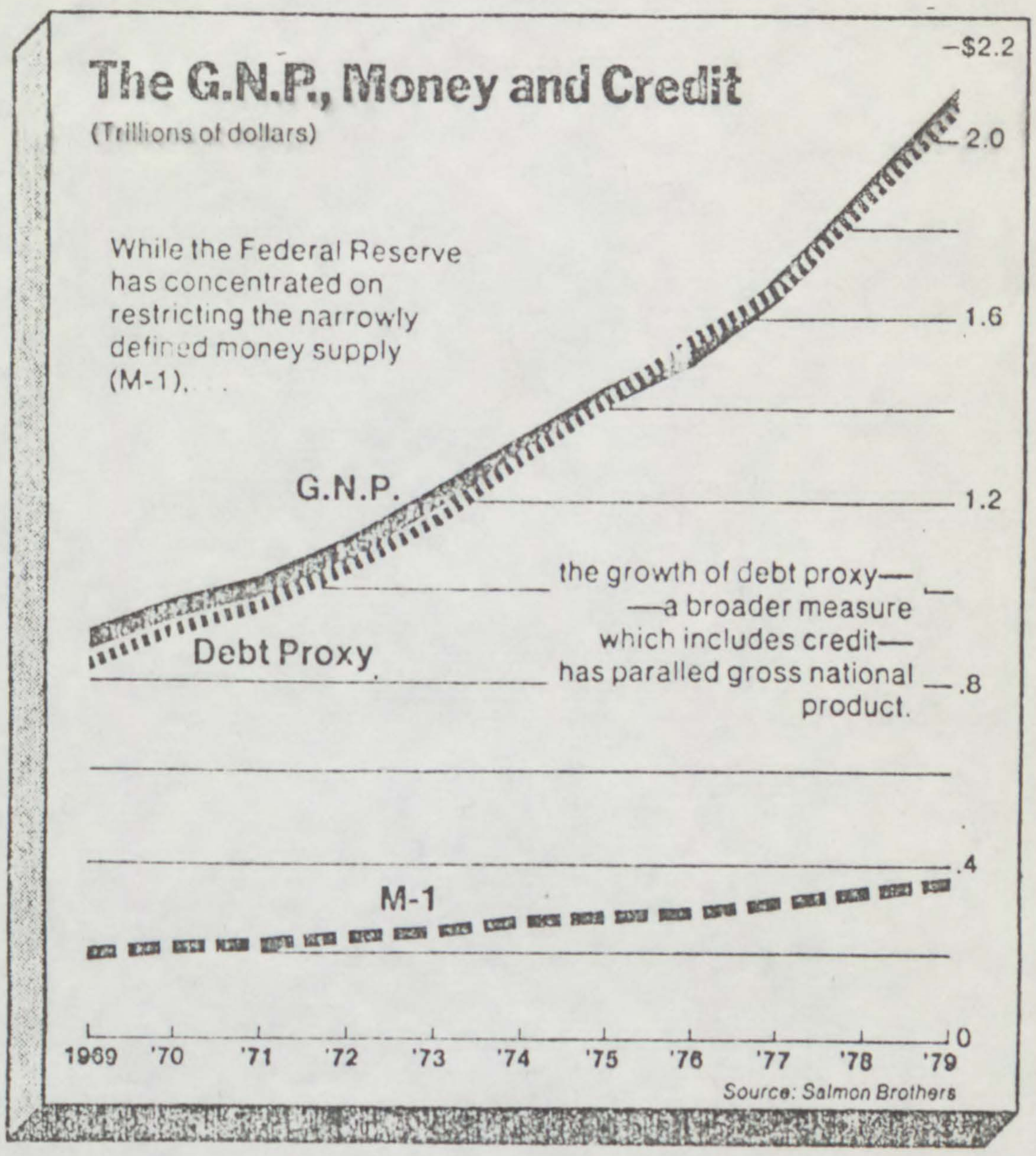


'Will the Fed continue to operate within a statistical jungle gym that allows it to play with small blocks of money?'

ticipation — namely, to know markets and the changes emerging in them. The Federal Reserve has persisted all these years in defining its money supply target along classical lines — currency, demand deposits, and, to some extent, time deposits.

Meanwhile, the economic participants in this country, whose activities the Federal Reserve is trying to influence, have changed their own concept of money by greatly expanding the definition. Consequently, their spending embraces many more variables than the Federal Reserve acknowledges in its conduct of monetary policy.

Business, households and even governments, in the conduct of their economic affairs, no longer distinguish between money and credit. In many transactions, money and credit are indistinguishable. Corporations believe that they have ready access to money through the standby fee they pay for an unused line of credit. They judge their liquidity not by cash in the bank but mainly by holdings of other liquid assets and their borrowing capacity. Individuals exercise their credit cards as if they were disbursing money. They judge their liquidity in part by how much they monetize the equity value of their homes.

The real story behind our severely aggravated inflation is that the growth of credit has been proliferating while the Federal Reserve has been focusing on the M-1 and M-2 money supplies. Total credit market debt outstanding (obligations of households, business and governments in the United States) totaled $720 billion at the end of 1960, increased by 94 percent to $1.4 trillion in 1970 and by 142 percent to $3.4 trillion in 1978. For these years, the outstanding stock of money (M-1) rose from $144 billion to $220 billion, an increase of 53 percent, and then by 64 percent to $361 billion. Contributing to this massive growth of debt has been, among other things, the removal of a variety of restrictions on financial markets such as interest-rate ceilings; the introduction of new financing techniques and credit instruments that permit new ways to create credit and debt, the minimization of the risks of changes in interest rates through the issuance of floating interest-rate obligations, and the increasing linkages with international credit markets.

When access to worldwide credit is easy, who needs the money that the Federal Reserve is watching?

Credit markets today are the antithesis of what they were a few decades ago. Today, credit markets find ways to accommodate the inflationary process and, in fact, are helping to finance inflation. A decade ago, these markets were part of the disciplinary force.

The Federal Reserve, had it been sensitive to the ingenuity of the credit markets and to the rapid growth of debt, would have complemented its narrow target for money growth with a broadly based target for credit growth. If it had done so, the Federal Reserve would have perceived long ago that its monetary and interest-rate policies were incorrect, because they favored borrowing and consumption instead of savings and investment. During the past six years, the inflation rate, as measured by the Consumer Price Index, exceeded on average the Federal funds rate (the official target of monetary policy) by 112 basis points. This is in sharp contrast to the 1960-73 period when the reverse was true, and the funds rate exceeded the inflation rate on average by 170 basis points per year. One need not be an economist to conclude that it pays to borrow under the interest rate policy that the Federal Reserve has pursued in recent years.

Recognizing that the destiny of our economy is entwined with the future effectiveness of monetary policy, it is fair to ask: Will the Federal Reserve continue to operate within a statistical jungle gym that allows it to play with small blocks of money, or should it be held accountable for the management of a highly innovative and at times destabilizing credit system that is now a reality?

The monetarists, after admitting the recent shortcomings of the money supply concept, generally favor patching it by adding some of the recent innovations to the classical definition of money. I would go much farther and urge that a monetary policy target comprising the growth of total debt be given equal weight. I propose that this target consist of private domestic nonfinancial holdings of credit market instruments plus deposits and currency. This target, which I call the "debt proxy," totaled $2.2 trillion in outstandings at the end of 1978 and parallels closely nominal gross national product, as the chart shows.

In the absence of a stirring debate on the targets of monetary policy, the monetarists and established bureaucracy may have their way. A patch will probably be put on a failing concept.

More than 100 years ago, the famous economist, John Stuart Mill, said: "The purchasing power of an individual at any moment is not measured by the money actually in his pocket, whether we mean by money the metals, or include bank notes. It consists, first, of the money in his possession; secondly, of the money at his banker's, and all other money due him and payable on demand; thirdly, of whatever credit he happens to possess."

In our time, Milton Friedman said that money matters. The question is: "What is money?"

Henry Kaufman is a partner and member of the executive committee of Salomon Brothers.

Another Way to Count the Mo

Continued from Page 1

tween money supply and economic activity works both ways. What then has gone wrong? The monetary authorities submit a partial explanation for the inflation problem by calling attention to many events and forces beyond their control that have contributed to the current malaise. They cite an overly expansionary fiscal policy of sizable Federal deficit spending that makes it difficult to limit money supply growth without, as a result, denying substantial funds to the private sector. They point to such exogenous factors as the decision of the oil-producing nations to raise sharply the price of oil, and poor crop harvests abroad. Such exogenous forces and so-called non-monetary developments cannot be denied, but they also do not really excuse poor monetary performance.

In fact, the general belief that higher oil prices are the primary cause of our inflation is without foundation. In the past year, the Consumer Price Index has risen 11.5 percent. Excluding higher energy costs, the index has gone up 9.4 percent.

The monetarists state that the Federal Reserve failed to keep money supply growth, as measured by M-1, within the officially targeted range. Statistically, this is a correct observation, as shown in the table below:

M-1: Offical Growth Targets Vs. Actual Growth Rate

Period	Target (%)	Rate (%)
4/75-4/76	4½-7½	5.8
4/76-4/77	4½-6½	7.9
4/77-4/78	4-6½	7.2
4/78-4/79	1½-4½	4.5*

*First 8 months of 1979

Regrettably, though, this is not the answer, for if it were, the solution would be relatively simple. Even if the Fed had stayed within the guidelines, the small adjustment would hardly have had a significant impact on the inflation rate.

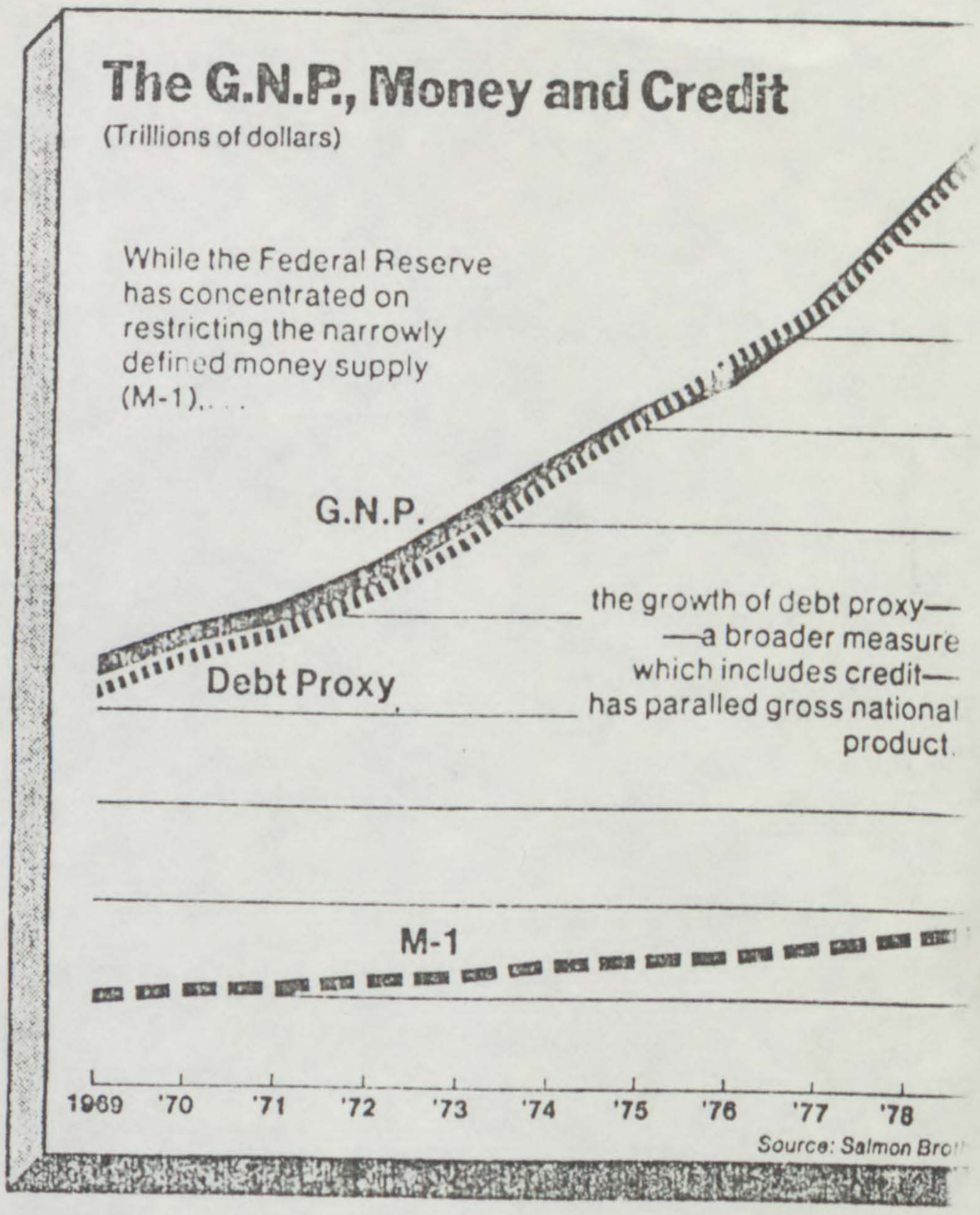
In assessing what has gone wrong, I believe that the failure of monetary policy lies in the Federal Reserve limiting its target to the narrow statistical concept of the money supply.

Think of the problem in these terms: The narrowly defined money supply, M-1, (demand deposits and currency) totals $375 billion and the broadly defined money supply, M-2, (demand deposits, currency and time deposits) totals $925 billion as compared with a nominal gross national product of $2.3 trillion. As shown in the accompanying chart, nominal gross national product has grown more rapidly than the money supply defined as M-1. The monetarists explain this growing gap between money and G.N.P. by pointing to the increase in money velocity — that is, the rate at which money is turned over, or spent and respent, in a year. However, the growth of velocity is not steady, but varies considerably over a business cycle.

Actually, what has really happened is that the Federal Reserve has failed in the cardinal principle of market participation — namely, to know markets and the changes emerging in them. The Federal Reserve has persisted all these years in defining its money supply target along classical lines — currency, demand deposits, and, to some extent, time deposits.

Meanwhile, the economic participants in this country, whose activities the Federal Reserve is trying to influence, have changed their own concept of money by greatly expanding the definition. Consequently, their spending embraces many more variables than the Federal Reserve acknowledges in its conduct of monetary policy.

Business, households and even governments, in the conduct of their economic affairs, no longer distinguish between money and credit. In many transactions, money and credit are indistinguishable. Corporations believe that they have ready access to money through the standby fee they pay for an unused line of credit. They judge their liquidity not by cash in the bank but mainly by holdings of other liquid assets and their borrowing capacity. Individuals exercise their credit cards as if they were disbursing money. They judge their liquidity in part by how much they monetize the equity value of their homes.



'Will the Fed continue to operate withi a statistical jungle gym that allows it to play with small blocks of money?'

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When access to worldwide c easy, who needs the money t Federal Reserve is watching?

Credit markets today are the a sis of what they were a few d

October 24, 1979

The Honorable Henry S. Reuss
House of Representatives
Washington, D.C. 20515

Dear Mr. Reuss:

Thank you for your letter of October 9 regarding Mr. Henry Baumhaf's concern with the accuracy of the Federal Reserve's weekly reports on gold reserves.

The figures in the Federal Reserve's weekly consolidated statement of condition represent the value of gold certificates issued to the System by the Treasury, at the legal valuation of $42.22 per fine troy ounce. While the fineness of the Treasury's gold is not uniform, because the stock includes melted coins and other forms of gold containing alloys, the valuation is applied only to the fine gold content of the gold stock. Thus, although not all the gold is in "good-delivery" form, the valuation of the gold is not overstated in the Federal Reserve's accounts.

In regard to the need for enactment of H.R. 3862, I understand that more than half the Treasury gold stock has already been inventoried under procedures acceptable to the General Accounting Office, in a survey that the Treasury has been conducting since 1974.

I hope that these comments will be useful to you.

Sincerely,
S/Paul A. Volcker

DBA:EMT:JPB:pjt (#V-70)
bcc: Mr. Truman
Mr. D. Adams
Mrs. Mallardi (2)

HENRY S. REUSS
5TH DISTRICT, WISCONSIN

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Congress of the United States
House of Representatives
Washington, D.C. 20515

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CHAIRMAN
JOINT ECONOMIC COMMITTEE
INTERNATIONAL ECONOMICS SUBCOMMITTEE
CO-CHAIRMAN

OCT 12 10:28

October 9, 1979 #70

The Honorable Paul Volcker
Chairman
Federal Reserve System
Twentieth Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Paul:

My friend, Henry Banzhaf, of Milwaukee has written to me in support of H.R. 3862, Congressman Ron Paul's bill to authorize a full audit and inventory of United States gold reserves. One of his arguments for passage of the bill is that the Federal Reserve's weekly reports on gold reserves are inaccurate. He states that the Fed "does not take into account the large percentage (of gold) which is in alloy less than the acceptable monetary standard" and that, according to the Treasury Department, "only about 18 million ozs. of the gold reserve are good delivery gold".

I would welcome your comments on this.

Sincerely,

Henry

Henry S. Reuss
Member of Congress

October 24, 1979

The Honorable Jerry M. Patterson
House of Representatives
Washington, D.C. 20515

Dear Mr. Patterson:

Thank you for your letter of October 18, requesting the Board's comments on your proposed substitute to H.R. 2255 that would, among other things, amend section 4(c)(8) of the Bank Holding Company Act to provide that the underwriting and sale as agent of credit-related accident, life and health insurance, and property and casualty insurance on collateral securing an extension of credit by a nonbank subsidiary of a bank holding company, are activities "closely related" to banking. In addition, your proposal provides that a borrower has a right to cancel insurance offered by a bank holding company or its subsidiary in connection with an extension of credit within 30 days after the insurance has been purchased, provided certain other conditions are met.

The Board believes that government regulation should have the effect of fostering competition, and it is the Board's opinion that it encouraged competition when it authorized bank holding companies to engage in certain insurance activities under section 225.4(a)(9) of Regulation Y. While H.R. 2255 would substantially reduce competition between the banking and insurance industries, your proposal would restore some of that competition the Board sought to encourage by adopting section 225.4(a)(9). The Board believes that Congressional circumscription of a specific section 4(c)(8) activity removes the flexibility present in proceeding by regulation, which is necessary to accommodate changing times and circumstances. We note that your proposal would have the effect of precluding bank holding companies from engaging as agent in currently permissible insurance activities, such as selling property and casualty insurance for the bank holding company and its subsidiaries and would prevent a nonbank subsidiary of a bank holding company from acting as agent in connection with extensions of credit by affiliated bank and nonbank subsidiaries. Finally, your proposal appears to authorize the underwriting of property and casualty insurance by bank holding companies, and we note that the Fourth Circuit Court of Appeals upheld the Board's determination that such activity is not "closely related" to banking within the meaning of section 4(c)(8) of the Act. NCNB vs Board of Governors 599 F.2d 609 (1979).

With respect to section 3 of your bill, which would add a new section 13 to the Bank Holding Company Act, the Board feels this provision would eliminate to a significant degree the concerns with tie-ins that have resulted from a bank holding company subsidiary offering to the borrower both a loan and insurance on the loan.

Thank you for this opportunity to comment and please feel free to contact me if any further information is necessary.

Sincerely,

S/Paul A. Volcker

RW:MEB:RM:pjt (#V-83)
bcc: Rich Whiting
Mike Bleier
Bob Mannion
Mrs. Mallardi (2)

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
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JERRY M. PATTERSON
38TH DISTRICT OF CALIFORNIA

Congress of the United States
House of Representatives
Washington, D.C. 20515

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WASHINGTON, D.C. 20515
TELEPHONE: (202) 225-2965

#83

October 18, 1979

The Honorable Paul Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

Enclosed is a copy of my proposed substitute to H.R. 2255 as reported by the Financial Institutions Subcommittee on September 11th. I invite the Board to comment on this proposal, which will be considered by the Banking Committee next week.

With best personal regards,

Sincerely,

Jerry Patterson

JERRY M. PATTERSON
U.S. Congressman

JMP/lln
Enclosures

AMENDMENT IN THE NATURE OF A SUBSTITUTE

TO H. R. 2255

OFFERED BY MR. PATTERSON

Strike out all after the enacting clause and insert in lieu thereof the following:

That this Act may be cited as the ''Bank Holding Company Act Insurance Amendments of 1979''.

SEC. 2. Section 4(c)(8) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(c)(8)) is amended by striking out the period at the end of the first sentence and inserting in lieu thereof the following: '', but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent, or broker, except (A) where the insurance is limited to assuring repayment of the outstanding balance due on a specific extension of credit by a bank holding company or its subsidiary in the event of the death or disability of the debtor; (B) in the case of a non-bank subsidiary of a bank holding company, where the insurance is also limited to insuring the collateral on a specific extension of credit by such non-bank subsidiary in the event of loss or damage to, or from the use of, any property used as collateral on such extension of credit, except that such non-bank subsidiary may only act as an agent or broker; (C) that a bank holding company may conduct any insurance agency activity in any place that (i) has a population of not more than five thousand (as shown by the last preceding decennial census), or (ii) the bank holding company, after notice and opportunity for a hearing, demonstrates has inadequate insurance agency facilities; (D) any insurance agency activity that was lawfully engaged in by (i) a bank holding company or any of its subsidiaries on June 6, 1978, or (ii) a finance company which became a subsidiary of a bank holding company through acquisition during the period beginning on June 6, 1978, and ending on June 6, 1979.''.

SEC. 3. The Bank Holding Company Act of 1956 (12 U.S.C. 1841 et seq.) is amended by adding at the end thereof the following new section:

''INSURANCE RESTRICTIONS

''SEC. 13. (a) With respect to any extension of credit to any person by a bank holding company or any of its non-bank subsidiaries, the bank holding company or non-bank subsidiary involved may require such person to purchase insurance coverage for loss or damage to, or from the use of, the property used as collateral in such extension of credit, except that, as a condition for such extension of credit, such bank holding company or non-bank subsidiary shall not require such person to purchase such insurance from any source specified by such bank holding company or non-bank subsidiary .

''(b) With respect to any extension of credit to any person by a bank holding company or its non-bank subsidiaries, no such bank holding company or non-bank subsidiary may provide the insurance described in subsection (a) as an agent or broker unless--

''(1) the contract incorporating such insurance provides--

''(A) that such person has the right to cancel such insurance in any case in which, not later than 30 days after the date on which such insurance is purchased, such person mails or delivers a notice to such bank holding company or non-bank subsidiary and such notice--

''(i) requests the cancellation of such insurance as of the date on which such notice is mailed or delivered to such bank holding company or non-bank subsidiary;

''(ii) specifies the name and address of the new source from which such person has secured the insurance described in subsection (a); and

''(iii) demonstrates that the insurance provided by such new source will take effect at or before the time at which the coverage of the existing insurance terminates;

''(B) that such cancellation notice shall automatically take effect as long as such notice is submitted pursuant to subparagraph (A) and the new source of insurance specified pursuant to subparagraph (A)(ii) is licensed by the State in which such person resides to sell such insurance in such State; and

''(C) that, after submitting a notice, pursuant to subparagraph (A), which satisfies the requirements of subparagraph (B), such person shall receive a refund of all premiums which have been paid by such person for such insurance and of all premiums which have been financed by such person for such insurance; and

''(2) at the time of such extension of credit, such person is given a written notice which is not part of any document involving such extension of credit and which contains a clear and conspicious statement--

''(A) that such insurance is being purchased in connection with an extension of credit;

''(B) of the cost of such insurance;

''(C) detailing the cancellation provisions of paragraph (1); and

''(D) of the address to which any cancellation notice submitted pursuant to paragraph (1)(A) shall be mailed or delivered.''.

SEC. 4. This Act shall take effect ninety days after the date of the enactment of this Act.

October 23, 1979

The Honorable William Proxmire
Chairman
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Proxmire:

Thank you for your letter of October 18 which requests the Board's views on an amendment which may be offered to H.R. 4986 which would delete the reserve requirement provisions of the bill to the effect that the Board could only apply reserve requirements to ATS and NOW accounts at member banks. The Board strongly opposes such an amendment.

As you know, the Federal Reserve has been facing a serious and accelerating loss of members. This membership attrition is related directly to the inequitable reserve burden that member banks presently carry. We have been actively seeking a legislative solution to this problem for more than three years.

The amendment which may be offered would aggravate the problem.

The bill which is under consideration by the U.S. Senate looks to authorize a new service for most of our nation's financial depository institutions. In turn, the amendment looks to impose a reserve requirement burden on only a limited category of institutions which would be authorized to offer the new service--namely, banks that are members of the Federal Reserve. If such an additional burden is imposed on member banks only, the already considerable pressures to leave the Federal Reserve System would be increased for many of our nation's banks.

I have a certain degree of sympathy for the argument made by Senator Morgan that this reserve issue be settled in the context of legislation which addresses all aspects of the Fed membership problem. The Federal Reserve under three Chairmen has been seeking such legislation, and we will continue to seek it. However, in the interim period the Congress should not adopt legislative measures which would only exacerbate the serious membership problem we are facing which already is eroding the precision with which we can implement monetary policy while creating serious competitive inequities within the financial system.

I hope that the Senate will not adopt this amendment and maintain the wording of the bill as reported out of the Senate Banking Committee which requires that NOW accounts, share draft accounts and ATS accounts at all depository institutions be subject to uniform reserve requirements set by the Board of Governors of the Federal Reserve. Ultimately, I continue to hope that the reserve requirement matter can be settled in the context of broader legislation, but I also trust the matter will not be further aggravated by failure to keep the reserve requirement provisions of H.R. 4986.

Sincerely,

S/Paul A. Volcker

KAG:PAV:pjt (#V-82)
bcc: ~~XXXXX~~ Mrs. Mallardi (2)

United States Senate
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, D.C. 20510

#82

October 18, 1979

The Honorable Paul A. Volcker
Chairman, Board of Governors of
the Federal Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

The legislation recently approved by the Senate Banking Committee (H.R. 4986) would authorize nationwide NOW accounts (except for Federal savings and loans in California), share drafts, and automatic transfer savings accounts. Title II of the legislation authorizes the Federal Reserve to impose reserve requirements on such accounts within a broad range. The authorization would be for mandatory and uniform reserves on such accounts for all depository institutions and reserves would be maintained in a form consistent with the Board's past reserve requirement proposals to the Congress.

I understand that an amendment will be offered on the Senate floor to delete the reserve requirement provisions of the legislation, so that the Board could only apply reserve requirements to NOW and ATS accounts at member banks. I would like to know the Board's views on eliminating the reserve requirements provision of H.R. 4986 for NOWs, share drafts, and ATS accounts at nonmember banks and thrift institutions.

Sincerely,

Bill Proxmire

William Proxmire
Chairman

WP:srl

1979 OCT 18 PM 3:57

UNIVERSITY OF OREGON

an equal opportunity affirmative action employer

College of Business Administration
JOHN B. ROGERS PROFESSOR
OF BANKING AND FINANCE

EUGENE, OREGON 97403
telephone (code 503) 686-3381

October 25, 1977

Congressman Henry S. Reuss, Chairman
Committee on Banking, Finance and Urban Affairs
U.S. House of Representatives
B301C Rayburn House Office Building
Wasbington, D.C. 20515

Dear Congressman Reuss,

This is in response to your request through Mr. Robert Auerbach for evaluation of the Board's October 6, 1977. report "Analysis of the Impact of Lagged Reserve Accounting".

I have read the Board's report, and my principal conclusion is that it is not addressed to the major question that I believed you asked, namely "how has lagged reserve accounting affected the ability of the Fed to achieve its target growth rates in monetary aggregates?" Instead, the report primarily analyzes the effects of lagged reserves on variability in Fed funds rates and in monetary aggregates. I have no major disagreements with the report on these sections. I will comment on the report in the same order as the conclusions are presented on pages 1 through 3.

1. I have no evidence on cost savings to banks from lagged reserve accounting and will accept the results of the Board's survey, although it appears to be rather casual. The effect on membership was one of the major reasons for adopting lagged reserve accounting initially.

2. The effect of lagged reserves on the variability of Fed fund rates is not relevant for dynamic monetary control. The finding that the variability increased after the introduction of lagged reserves is contrary to what was predicted in the 1966 System Report (Black Report). The fact that "enlarged defensive open market operators offset this tendency" raises the question of the cost-benefit ration of such operations. Defensive operations are not free to the economy, particularly when they reach $450 billion as they did in 1976. Of course, all of this increase is not attributed to lagged reserves. A large part reflects the change in the management of Treasury balances. Nevertheless, if lagged reserves require significantly higher defensive operations, this cost should be considered.

3. Likewise, the effect of lagged reserves on the variability in M1 and M2 is not directly relevant to the principal question.

4. I disagree that the "choice between lagged or contemporaneous accounting is of relatively little significance" for the Fed's ability to achieve its growth targets in M1 and M2 even under its current operating procedures. Under concurrent reserve accounting (CR), the Fed can change, say reduce, bank deposits (and thereby monetary aggregates) by selling securities on the open market. This reduces bank reserves. Banks respond by contracting deposits immediately to levels consistent with the available reserves. Under lagged reserve accounting (LR), required reserves in a reserve week are set to the dollar by deposits two weeks earlier. They cannot be changed by either the banks or the Fed. Thus, 1) in any reserve period banks can change deposits without regard to reserves in the same period and 2) open market sales cannot reduce either aggregate required reserves or aggregate deposits in the same week. Open market sales will affect only the mix of reserves between borrowed and unborrowed.

As long as the Fed accommodates changes in money demand or non-Fed supply factors to maintain interest rates, CR and LR yield similar effects. But what happens when the Fed wishes to resist changes in money demand? Under CR, the Fed contracts reserves, and deposits follow. Deposits are now supply determined. Under LR, reserves cannot be contracted in the same week as the Fed must provide all the reserves that the banks require to support their deposits of two weeks earlier, either through open market operations or the discount window. The Fed can change deposits and thereby required reserves from demand determined to supply determined only by signalling to the banks that there will be a higher cost of reserves two weeks hence when the banks need the reserves to satisfy this week's deposits and required reserves. As the future cost of reserves increases, ceteris paribus, the banks will reduce deposits now.

Thus, LR changes the cutting edge of dynamic monetary control from open market operations to discount management. A higher reserve cost in the future may be signalled by either or both an increase in the nominal discount rate or an increase in the effective rate through a more restrictive discount administration. Without this, deposits remain demand determined. (The reluctance to signal a sufficiently high future cost of reserves can account for the more rapid than target growth rate in monetary aggregates in recent periods.) If the Fed is reluctant to use the discount mechanism to signal changes in costs, the choice between CR and LR matters even under current operating procedures. LR introduces a procyclical bias into monetary control. I enclose pages 533-34 from my textbook, Money, The Financial System and the Economy (second edition), which expands on this argument.

5. I concur with this conclusion except for the statement that CR would result in "unprecedented short-run variability in the funds rate." There is at least some evidence that in the absence of Fed defensive operations, the private sector will smooth out the short-run interest rate volatility. Moreover,

it appears that it currently requires an "unprecedented" volume of defensive operations to avoid "unprecedented" variability in the Fed funds rate.

6. The study uses the wrong measure for gauging the effectiveness of CR or LR for longer-run monetary control. Rather than variability in either rates or aggregates, the relevant measure is variability in the difference between the targeted and realized rates of monetary growth.

In sum, there is nothing in the Board's report to indicate that lagged reserves have not weakened the Fed's ability to attain its target growth rates in monetary aggregates.

Sincerely,

George Kaufman

George G. Kaufman

GGK:sd

Enclosures

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

G. WILLIAM MILLER
CHAIRMAN

RECEIVED
MAY 2 1978
Banking, Finance & Urban Affairs Committee

May 1, 1978

The Honorable Henry S. Reuss
Chairman
Committee on Banking, Finance
and Urban Affairs
House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

Thank you for your letter of April 18 conveying further views on lagged reserve accounting. By now, considerable work on the subject has been undertaken by our staff and by economists more generally. The issues involved appear to be clear, though judgments about the importance of the whole question may well differ.

As you know, the Board has been carefully reviewing actions that might be taken to make membership in the Federal Reserve System less burdensome. As part of this effort, the Board may also be in a position to reassess the desirability of lagged reserve accounting.

Sincerely,

Bill

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

2129 RAYBURN HOUSE OFFICE BUILDING

WASHINGTON, D.C. 20515

June 21, 1978

The Honorable G. William Miller
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Mr. Chairman:

Thank you for your prompt replies on the subjects of doing away with lagged reserve requirements and staggering the reserve settlement dates contained in your May 1 and June 16 letters.

In your May 1 letter you indicated that the Board may also be in a position to reassess the desirability of lagged reserve accounting. Would you let me know if this issue has been considered by the Board and, if not, when it will be considered. I would also like to be informed of the Members' views on this important issue of monetary control.

In your June 16 letter you indicate that the subject of staggered settlement dates has been much discussed over the years. Would you send me all pertinent reports and studies that have been done since the Federal Reserve received Milton Friedman's 1965 detailed Memorandum strongly supporting staggered reserve accounting. This will be very useful to me and to the scholars I have consulted on this issue. I would also like to be kept informed of the review that you indicate in your June 16 letter your staff will now undertake of this issue. The cost of the massive churning of the Federal Reserve portfolio, to the tune of $1.2 trillion in 1977, as well as the effect of this churning on the obligation of the Federal Reserve to monitor the money supply as well as interest rates deserves immediate attention.

I am deeply interested in anything that can be done to improve the Federal Reserve's ability to bring down interest rates and better control the money supply.

Sincerely,

Henry S. Reuss

Henry S. Reuss
Chairman

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-FIFTH CONGRESS

2129 RAYBURN HOUSE OFFICE BUILDING

WASHINGTON, D.C. 20515

225-4247

August 10, 1978

The Honorable G. William Miller
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Miller:

Your testimony on July 27 and 28 contributed importantly to the Committee's understanding of the Fed's current monetary policy and to our deliberations on legislation to improve monetary control and resolve the membership problem. We have, as you know, developed legislation, the Federal Reserve Act Amendments of 1978, which resolves the membership problem and facilitates the Federal Reserve's ability to conduct monetary policy.

I would like to call your attention to four problems related to monetary control, and make one suggestion for improving the Federal deficit, all of which I believe the Federal Reserve can effectively deal with through regulatory provisions.

The first problem is the failure of the Federal Reserve to present target ranges for M1 which it intends to live within. This is an issue with which we are both concerned, because the failure by the Federal Reserve for more than a year now to keep M1 within its announced growth target range has had unfortunate monetary effects, both at home and abroad. The Federal Reserve's response that its current M1 target range starts from a high base, and therefore is more realistic than it appears, in no way alters the fact that it is misleading. I recommend, as I have before, that for the immediate future, the Fed fix its M1 limit at a level consistent with our nation's goal of a healthy economy and stable dollar, and then stick to it.

The second point concerns the elimination of lagged reserve requirements and the reinstitution of synchronous reserve requirements. I was cheered by your statement in our hearings on July 28 that "in terms of operation it would be preferable to be on a current basis". You indicated that you would make the change to synchronous reserve requirements "once we can alleviate some of the membership problems." The proposed legislation, the Federal Reserve Act Amendments of 1978, would do just that.

I want also to call to your attention the comments of President Morris of the Federal Reserve Bank of Boston at our hearings on July 31, 1978, that he has been "an advocate of eliminating the lagged reserve requirements. I think we ought to move ahead in that."

The third problem is the Wednesday scramble in and out of reserves as every member bank in the United States is forced by Federal Reserve regulation to come up with the necessary reserve requirement for the preceding week at the close of business on Wednesday. In my June 21 letter to you on this subject, I asked for all pertinent reports and studies that had been done on this subject since the Federal Reserve received Milton Friedman's 1965 detailed memorandum strongly supporting staggered reserve accounting. On July 11, you sent me a staff study dated December 9, 1975, revised July 6, 1978, which seemed to indicate a problem with my suggestion that we adopt a system of staggered settlement dates so that 20 percent of the weekly reserve requirements could be settled on each week day. William Poole, Professor of Economics at Brown University, formerly a member of the staff of both the Board of Governors and the Boston Federal Reserve Bank, and currently an advisor to the Federal Reserve, has analyzed your staff study. His enclosed remarks conclude that rather than attacking a system of staggered reserve settlement dates, your staff memorandum actually "strengthens the case for such a system".

The fourth point concerns the discount rate. Currently, changes in the discount rate can be and often are misinterpreted. When other short term rates are falling, decreasing the discount rate can be interpreted as a sign that the Fed is easing when in fact it is only moving with the market. Vice versa, when other short term rates are rising, increasing the discount rate can be interpreted as a sign that the Fed is tightening when, again, it is only moving with the market. To make sure that changes in the discount rate are unambiguous, and also to minimize arbitrage possibilities, you could tie the discount rate to the Treasury bill rate, or the Federal funds rate or some index of short-term rates -- perhaps ¼ or ½ point above the formula rate -- except in unusual circumstances when there is good reason to send the financial community an unambiguous signal that the thrust of monetary policy is being changed. In those rare instances when a signal was needed, the Board, responding to initiatives from the Reserve Banks, would set the discount rate at a rate other than the one dictated by the formula, good for one week and renewable. If set above, it would be a clear signal that policy was being tightened. If set below, it would signal that policy was being eased. Needless to say, the Reserve Banks and Board would have to review and determine whether circumstances dictated setting the discount rate above or below the formula rate every week, even though the occasions for departing from the formula rate would be rare. Review and determination of the discount rate would, I believe, be far better focused under this procedure than presently.

My fifth point concerns the $1 billion plus surplus which is sitting in the Federal Reserve's attic, covered with dust, and serving no useful purpose. You have offered to dust off $575 million of the surplus and ship it over to the Treasury to offset part of the cost of solving the membership problem. Actually, of course, in a consolidated statement of government finances, the surplus would not exist and it would not affect the real income of our citizens in any meaningful way whether it was a bookkeeping entry at the Federal Reserve or at the Treasury. I do not think we should obscure the cost of the various legislative proposals by encumbering the calculations with shifts in the surplus. The transfer of the surplus to the Treasury will, however, make our deficit look smaller. Whatever psychic income this cosmetic benefit produces is surely preferable to allowing the surplus to gather further dust. Why not transfer the surplus in its entirety, at whatever rate your comptroller is able to adjust his books?

Let me thank you for your thorough testimony during two long days of hearings on July 27 and 28. Your comments have been very helpful in our deliberations.

Sincerely,

Henry

Henry S. Reuss
Chairman

Enclosure

BROWN UNIVERSITY Providence, Rhode Island - 02912

July 25, 1978

The Honorable Henry S. Reuss
Chairman
U. S. House of Representatives
Committee on Banking, Finance
and Urban Affairs
Ninety-Fifth Congress
2129 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Reuss:

I am replying to your letter of July 18, 1978, concerning the memorandum by Daniel Laufenberg on staggered reserve settlement periods.

Overall, I believe that the Laufenberg memorandum provides some insight into the economics of staggered reserve periods, and strengthens the case for such a system. The table on page 2 of the memorandum illustrates very nicely why staggered reserve periods would not lead to an effective evasion of monetary control. The increasing oscillations in reserves that show up in this table clearly could not continue for very many periods. In the middle of page 3 of his memorandum, Laufenberg dismisses the argument that the growing oscillations could not continue. His argument, however, is hardly convincing. For one thing, it is simply not true that banks pay no attention to the behavior of the banking system as a whole. His argument reminds me somewhat of the argument for a chain letter. A chain letter can continue so long as no one bothers to examine the implications, but in fact most people do understand the implications of chain letters and they don't go very far. Similarly, banks would surely understand the implications of the extreme oscillatory pattern shown on page 2 of the memorandum and would not permit that pattern to go very far.

Another important reason that the oscillatory pattern could not go very far is that banks lending federal funds pay attention to the credit worthiness of the borrower. Thus, banks would not be able to borrow the growing amounts shown in the table because other banks would refuse to lend such large amounts. Each individual bank, knowing that the supply of federal funds to it will be limited by the behavior of the lending banks, would take some action to dispose of assets long before the violent oscillations got very far along.

The table on page 5 of the Laufenberg memorandum provides a simple example of how staggered reserve periods might work when banks undertake to sell assets in order to adjust their reserve positions. The striking thing about the table is that the change in deposits is spread over a series of periods. It should be emphasized that with contemporaneous reserve requirements and no staggering of reserve settlement periods, the assumed decline of reserves of 10 in the first period would force an immediate decline of 100 in deposits under the assumptions employed in this example and assuming no Federal Reserve offsetting action. The Laufenberg table, in contrast, shows that the decline in deposits comes in a series of steps spread over time rather than all in one big swoop. It is surprising, therefore, that Laufenberg utilizes this example as indicating a potential problem with staggered reserve settlement periods.

The basis of Laufenberg's criticism of staggered settlement periods comes from solving the difference equation at the top of page 7. This equation is derived from the very simple assumptions which should be regarded as being useful for illustrative purposes. But surely it is a mistake to take an example set up for illustrative purposes and then to crank through its mathematical properties without paying any attention to how the model might be slightly off. When the simple model is solved the problem is that the solution involves indefinite oscillations in deposits, as emphasized by Laufenberg at the top of page 7.

The artificiality of this result can be demonstrated very easily. Suppose we go back to the simple assumption in the model at the top of page 6 as written down in equation (2). Underlying equation (2) is the notion that each bank would adjust its asset sales in order to exactly achieve its required reserve position, without making any allowance for holding excess reserves or any allowance for possible borrowing from the Federal Reserve. Suppose equation (2) is written in a slightly altered form which I will call (2a).

$$\text{(2a)} \quad \Delta D_t = 1.99\ (ER_{t-1} + .5\ \Delta D_{t-1})$$

Equation (2a) has the assumption that the bank covers practically all of a reserve deficiency, borrowing just a little from the Fed; or uses a reserve excess almost completely to purchase assets, but holds just a little uninvested to provide an excess reserve cushion. All I have done is to change the 2 in Laufenberg's equation (2) to 1.99 in my equation (2a). If this substitution is made and the resulting model solved it will be found that the system is still oscillatory but it is damped. Thus if equation (2a) rather than (2) were to discribe bank behavior, then the Laufenberg conclusion that deposits would increase, and then decrease, and so on indefinitely would be changed and the correct conclusion would be that the oscillations would dampen over time so that deposits would converge to their long-run equilibrium level.

The point of all this is not to say that equation (2a) is correct and equation (2) is incorrect; rather, it is to emphasize that a model of this type should be considered as illustrative and not as accurate enough that we would want to rely on its detailed mathematical properties. My considered opinion is that the illustrative model has the correct implication that the response of deposits to a reserve distrubance would be spread out over time to a greater extent than would the response under a conventional reserve system assuming that there is no Federal Reserve intervention. But to read more into this simple model is a grave mistake. There is no reason to believe that the actual behavior of the banking system would be anything other than very stable under staggered reserve periods system.

Finally, even if the staggered reserve system has some tendencies toward the instabilities identified by Laufenberg -- and I want to emphasize that I do not in fact believe that these instabilities exist -- Laufenberg's memorandum is seriously deficient in not making a proper comparison between the staggered reserve system and the present system. For one thing, any reasonable simple illustrative model of the present lagged reserve system will show much more violent instabilities under the same assumptions that Laufenberg has applied in his memorandum. Secondly, the actual system cannot be analyzed in the context of the assumption that the Federal Reserve never intervenes to smooth disturbances. The problem with the present system is that it magnifies and amplifies disturbances -- instead of damping them and spreading them out as staggered reserve periods would do -- requiring tremendous amounts of Federal Reserve activity to smooth out the disturbances caused by the current faulty regulations. Thus, the result of the present system, given the way the Federal Reserve behaves, is to generate the large continuing procyclical movements in the money stock that we have observed so often in the past and have been observing in recent months.

I hope my analysis of the Laufenberg memorandum has not been excessively long, but it is not a simple matter to explain exactly where Laufenberg's approach goes off base. Should you have any further questions please feel free to call on me again.

Sincerely,

William Poole

William Poole
Professor of Economics

WP:mem

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-SIXTH CONGRESS

2129 RAYBURN HOUSE OFFICE BUILDING

WASHINGTON, D.C. 20515

September 26, 1979

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Volcker:

The recent increase in the discount rate to 11 percent and the threat of even higher discount rates is in part a result of the method by which the Federal Reserve regulates the required reserves of member banks. The present system of lagged reserve requirements requires sharp increases in the discount rate in order to slow deposit expansion. If the lagged reserve requirement system is ended and the system used until September, 1968 -- concurrent reserve requirements -- was instituted the Federal Reserve would not need such high discount rates to bring the money supply under control.

Under lagged reserve requirements the Federal Reserve cannot slow down money growth through open market operations without throwing the member banks into deficient reserve positions which violate your regulations. The Fed is forced to control fast money growth by raising the discount and Federal funds rates higher than would be necessary under concurrent reserve requirements.

I am enclosing a recent letter from Professor George G. Kaufman, former Vice President of the Federal Reserve Bank of Chicago and currently the John B. Rogers Professor of Banking and Finance of the College of Business Administration at the University of Oregon. He emphasizes these points in relation to current Federal Reserve policy. "The recent apparently unintended acceleration in monetary growth appears to me to be attributable in part to lagged reserves. Further sharp increases in the discount rate will be needed to slow deposit expansion if loan demand remains strong. This strategy appears less desirable to me then a strategy of open market sales under concurrent requirements."

I would hope that the Federal Reserve could immediately switch to concurrent reserve requirements to avoid unnecessary increases in the discount rate.

Sincerely,

Henry S. Reuss

Henry S. Reuss
Chairman

Assigned to Steve Axilrod

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

NINETY-SIXTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515

225-4247

September 26, 1979 #49

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Volcker:

The recent increase in the discount rate to 11 percent and the threat of even higher discount rates is in part a result of the method by which the Federal Reserve regulates the required reserves of member banks. The present system of lagged reserve requirements requires sharp increases in the discount rate in order to slow deposit expansion. If the lagged reserve requirement system is ended and the system used until September, 1968 -- concurrent reserve requirements -- was instituted the Federal Reserve would not need such high discount rates to bring the money supply under control.

Under lagged reserve requirements the Federal Reserve cannot slow down money growth through open market operations without throwing the member banks into deficient reserve positions which violate your regulations. The Fed is forced to control fast money growth by raising the discount and Federal funds rates higher than would be necessary under concurrent reserve requirements.

I am enclosing a recent letter from Professor George G. Kaufman, former Vice President of the Federal Reserve Bank of Chicago and currently the John B. Rogers Professor of Banking and Finance of the College of Business Administration at the University of Oregon. He emphasizes these points in relation to current Federal Reserve policy. "The recent apparently unintended acceleration in monetary growth appears to me to be attributable in part to lagged reserves. Further sharp increases in the discount rate will be needed to slow deposit expansion if loan demand remains strong. This strategy appears less desirable to me then a strategy of open market sales under concurrent requirements."

I would hope that the Federal Reserve could immediately switch to concurrent reserve requirements to avoid unnecessary increases in the discount rate.

Sincerely,
Henry S. Reuss
Henry S. Reuss
Chairman

John B. Rogers Professor
of Banking and Finance
College of Business Administration
UNIVERSITY OF OREGON
Eugene, Oregon 97403

503/686-3381

September 7, 1979

Congressman Henry S. Reuss
Chairman, Committee on Banking, Finance
and Urban Affairs
U.S. House of Representatives
B301C Rayburn House Office Building
Washington, D.C. 20515

Dear Congressman Reuss,

Two years ago you requested me to comment on the effectiveness of lagged reserve requirements for Federal Reserve control of the money supply. In my letter dated November 18, 1977, I argued that lagged reserves impede the ability of the Fed to control the money supply. This view was not accepted by the Federal Reserve, in particular by Chairman Burns. In case you may not have seen it, I enclose a copy of an article entitled "Monetary Base Control" that is published in the June 1979 Quarterly Bulletin of the Bank of England. As in the U.S., reserve requirements in England are lagged. The authors conclude that "changes in deposits must cause the ~~authors~~ authorities to allow changes in bank reserves, and not vice versa, so that monetary base movements can hardly either control, cause or even indicate future movements in bank deposits." They suggest that if control of the money supply is to be the prime objective, concurrent or lead reserve requirements should be imposed. The latter scheme was recently proposed by Robert Laurent of the Federal Reserve Bank of Chicago.

The recent apparently unintended acceleration in monetary growth appears to me to be attributable in part to lagged reserves. Further sharp increases in the discount rate will be needed to slow deposit expansion if loan demand remains strong. This strategy appears less desirable to me then a strategy of open market sales under concurrent requirements.

Sincerely,

George Kaufman

George G. Kaufman

GGK:sjd

Enclosure

an equal opportunity/affirmative action employer

October 17, 1979

The Honorable Jim Sasser
United States Senate
Washington, D.C. 20510

Dear Senator Sasser:

I am pleased to respond to your recent letter regarding the effects of higher interest rates on inflation. Given the seriousness of our inflation problem, this certainly is an important question.

It is, in fact, not a new one; one can find it discussed in the economic literature of the nineteenth century. I believe it fair to say that the accumulated evidence--theoretical and empirical--points convincingly to the conclusion that, while rising interest rates that often accompany monetary restraint do add to costs and place some upward pressure on prices, this effect is small and overridden by the anti-inflationary impact of the moderation of aggregate demand fostered by higher interest rates. I might just mention two papers that have examined this specific topic:

> T. Humphrey, "The Interest Cost-Push Controversy," Federal Reserve Bank of Richmond Economic Review, January/February, 1979, pp. 3-10.
>
> S. Seelig, "Rising Interest Rates and Cost-Push Inflation," Journal of Finance, September, 1974, pp. 1049-1061.

The Humphrey article concludes that the great Swedish economist Knut Wicksell "provided the definitive critique" of the interest cost push doctrine, while the Seelig article presents a detailed industry-level econometric evaluation of interest cost impacts on prices. The findings of these authors are confirmed by other research as well, including informal investigations by staff at the Board of Governors.

High interest rates and rapid inflation are, to be sure, related phenomena. When inflation accelerates, lenders and borrowers alike anticipate the effects of rising prices on the purchasing power of eventual loan repayments. The result is higher nominal rates of interest. An attempt to overcome this tendency would require faster expansion of the money supply, but such a policy on the part of the central bank would very quickly prove counterproductive as the flood of additional dollars would lead to still greater inflation and stronger upward pressures on interest rates.

My colleagues and I on the Board are sensitive to the difficulties caused by higher interest rates. We very much would like to see a return to the lower rates that prevailed in the 1950s and early 1960s. Realistically, however, that cannot occur until inflation is brought down and a sense of stability is restored to the economy. I believe that the policies we have instituted, which are intended to achieve the needed moderation of monetary expansion, provide the best hope of attaining that goal. Of course, other governmental policies also have a part to play, and in this regard the efforts of the Senate Budget Committee to maintain fiscal discipline are to be commended.

Sincerely,

S/Paul A. Volcker

MJP:JLK:pjt (#V-62)
bcc: Mr. Kichline
Mr. Prell
Mrs. Mallardi (2)

Aissgned to Jim Kichline

JIM SASSER
TENNESSEE

ES:
TIONS
T
GOVERNMENTAL AFFAIRS

United States Senate

WASHINGTON, D.C. 20510

October 5, 1979

#62

Honorable Paul Volcker
Federal Reserve Board
Twentieth Street and
Constitution Ave. NW
Washington, D. C. 20551

Dear Mr. Chairman:

Interest rates in the United States have reached record highs at a time when the economy is clearly in a recession. Given the lags which are required to measure the extent of current restrictive policies and the extent of the economic decline in progress, I am really concerned that our monetary situation has become overly restrictive, and that a deep and prolonged recession may already be unavoidable.

As you know, inflation is still the principal problem we face today. Thus a restrictive fiscal policy is needed to reduce the inflationary effects of federal deficit spending. However, excessively restrictive monetary policy makes the task of fiscal discipline more difficult as output decreases and unemployment rises. If these policies are continued or extended, I do not hold out much hope to the taxpayers of this country for balancing the budget in 1981 as I had hoped.

You have recently announced your continuing commitment to a policy which allows interest rates to remain high, or go yet higher. I am disturbed by the potential consequences this policy carries for American working people. While I appreciate the need for concern about the international financial situation, I am deeply concerned about a policy which seeks to accomodate our foreign currency competitors at the expense of our own people. I do not think we should be allowing the burden of international monetary deficiencies to be carried on the backs of American farmers, small businessmen, and taxpayers. If a new international monetary system is needed to ease currency crises such as the one we now face, is the government pursuing actions to put one in place? What other options are available to improve the stability of the dollar? I want to be satisfied that this government is doing everything it can to reduce pressures on the dollar before resorting to even higher interest rates.

It seems to me that at some point, interest rates add to inflation, and to the depreciation of our currency, rather than to alleviate these problems. I believe we have already reached that point. Yet there is no measurement the government now makes which gives a comprehensive assessment of how interest rates affect the inflation rate. I fail to see how rational policies are possible without these data. Getting a better grip on the inflationary cost of rising interest rates will help the government and the private financial sector to determine the full consequences of our monetary policies.

Toward this end, I request that you look into two aspects of this matter. First, what is the best estimate of the effect of current market interest rates on today's inflation?

Second, what is the feasibility of establishing a new, comprehensive measure of the interest component in the inflation rate? It would be appreciated if this study addressed, but is not necessarily limited to, the following questions:

1. What are the existing methods by which government agencies measure interest costs in the economy?

2. What are the measureable ways in which interest costs can be recorded?

3. Since rising interest rates add to household and business costs, do they not add both to current

inflation and to inflationary expectations which serve to perpetuate high, and even rising, inflation?

I would appreciate your careful consideration of the questions I have raised, and look forward to your response.

Sincerely,

Jim Sasser

Jim Sasser
United States Senator

October 16, 1979

The Honorable Timothy E. Wirth
Member of Congress
8648 West Colfax Avenue
Lakewood, Colorado 80215

Dear Mr. Wirth:

Thank you for your letter of October 1, regarding difficulty encountered by your constituent, Mr. Joseph Cain, in obtaining a loan from Capital Federal Savings in Denver.

By statute, the Board's primary supervisory jurisdiction is limited to banks which are members of the Federal Reserve System. Primary supervisory authority over Federally chartered savings and loan associations remains with the Federal Home Loan Bank Board. Accordingly, I am referring your request to that agency for reply.

Sincerely yours,

(Signed) Donald J. Winn

Donald J. Winn
Special Assistant to the Board

cc: Congressional Liaison Office
Federal Home Loan Bank Board

CO:smk (#V-71)
bcc: Mrs. Mallardi ~~(2)~~

TIMOTHY E. WIRTH
2D DISTRICT, COLORADO

COMMITTEES:
BUDGET
INTERSTATE AND FOREIGN COMMERCE
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AIR FORCE ACADEMY BOARD OF VISITORS

CONGRESS OF THE UNITED STATES
HOUSE OF REPRESENTATIVES
WASHINGTON, D.C. 20515

WASHINGTON OFFICE:
312 CANNON HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-2161

DISTRICT OFFICE:
8648 WEST COLFAX AVENUE
LAKEWOOD, COLORADO 80215
(303) 234-5200

October 1, 1979

#1171

Mr. Paul Volcker, Chairman
Federal Reserve System
Board of Governors of the Federal Reserve System
Twentieth Street and Constitution Avenue Northwest
Washington, D.C. 20551

Dear Mr. Volcker:

A constituent, Mr. Joseph Cain, has contacted me complaining that Federal banking regulations create difficulty in obtaining loans for energy conservation.

Mr. Cain talked to Capital Federal Savings in Denver about a loan to purchase storm windows for five rental units. Capital Federal said banking regulations required separate loans for each unit.

Since the loans cannot be combined into one large figure, Mr. Cain would have to repay the loan over a much shorter term. A shorter term, of course, would mean higher monthly payments and Mr. Cain said his cash flow will not allow him to meet such high payments.

I would appreciate your attention to this matter and any assistance you can offer. Please direct any correspondence to my Colorado District Office at 8648 West Colfax Avenue, Lakewood, Colorado 80215.

With best wishes,

Sincerely ~~yours~~,

Tim Wirth

Timothy E. Wirth

TEW:scr

October 16, 1979

The Honorable Paul E. Tsongas
Chairman
Consumer Affairs Subcommittee
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Tsongas:

I am pleased to enclose the attached responses to your September 26, 1979 letter. I will forward the information your staff subsequently requested as soon as possible.

If you or your staff have any questions regarding the attached responses, please contact Jeannine Catalano, Review Examiner, at (202) 452-3946.

Sincerely,

S/Paul A. Volcker

Attachments

JC:smk (#V-47)
bcc: Jeanine Catalano
Catherine Mallardi(2)

Action assigned Janet Hart

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, D.C. 20510

September 26, 1979 ~~#46~~ #47

The Honorable Paul A. Volcker
Chairman, Board of Governors of the
Federal Reserve System
Washington, D.C. 20037

Dear Chairman,

In order to prepare for the Consumer Affairs Subcommittee hearings on October 16th and 17th, I would very much appreciate the following information from the Federal Reserve Board.

1. What constituted a reimbursable Truth-In-Lending violation from January 1969 to December 1978?

2. From January 1969 through December 1978, how many violations of Truth-In-Lending were identified?

   a. substantive vs. technical
   b. reimbursable vs. non reimbursable
   c. by year
   d. by region

3. How many and what amount of reimbursements for Truth-In-Lending violations were made from January 1969 through December 1978: by year, by region?

4. How many reimbursable violations were identified but never pursued during this period: by year, by region?

5. On what date did the FRB implement the uniform guidelines: by examination, by enforcement?

6. How many financial institutions have been examined for Truth-In-Lending by the FRB, since the uniform guidelines were implemented?

7. What sampling technique did the FRB use?

   a. sample size
   b. statistical or judgemental selection
   c. universe (one month, one year or back to October 1974)

   Did this vary by region, if so -- how?

8. How many reimbursable violations, under the uniform guidelines (as of August 1, 1979), are known to the FRB?

   a. the number of institutions having reimbursable violations, by region
   b. dollar amount of reimbursements, by region, if guidelines (as of August 1, 1979) were enforced.

9. Of the total reimbursable violations identified (8 b above) how many and what amounts have been reimbursed, by region?

10. Of total reimbursable violations found, as of August 1, 1979, what percent were principally attributable to:

    a. understated APR
    b. understated finance charge
    c. credit life insurance practices
    d. late payment or prepayment penalty practices

11. Of the possible reimbursement orders (as of August 1, 1979) how many have been issued, by region?

12. Of the reimbursement orders issued, how many have been completed?

13. How does the FRB verify that complete reimbursement has been made?

I would appreciate a response from the FRB by October 10th.

Sincerely,

Paul Tsongas

Paul E. Tsongas, Chairman
Consumer Affairs Subcommittee

October 16, 1979

The Honorable William Proxmire
Chairman
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D. C. 20510

Dear Chairman Proxmire:

In your letter of October 3, you called my attention to a Business Week editorial urging that the Federal Reserve change its operating procedures. As you know, the FOMC's policy actions of October 6 moved us in that direction and we discussed the issue in detail before the Senate Banking Committee on Monday. I trust that my comments before your Committee have answered the questions raised in your letter.

Sincerely,

S/Paul A. Volcker

ECE:KAG:vcd (#V-57)

bcc: Mr. Ettin
Mrs. Mallardi (2)

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, D.C. 20510

October 3, 1979

#57

The Honorable Paul A. Volcker
Chairman, Board of Governors of the
Federal Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

Last Friday's issue of Business Week contained an editorial critical of the Federal Reserve's monetary policy actions. I call this to your attention not because I concur in the view taken by the editorial. Rather, I think the editorial raises some interesting issues that the Federal Reserve should address. Therefore, I would like to have you or your staff comment on the points raised which are as follows:

First, the editorial suggests that the Fed can set whatever rate of money growth it wants simply by metering out reserves to support that amount of expansion and no more. Thus, what I take Business Week to be suggesting is that the Fed change operating procedures and peg the rate of growth of bank reserves rather than pegging interest rates.

Second, the editorial suggests that the Federal Reserve cannot curb credit growth by raising interest rates. In fact, raising interest rates are said to yield perverse responses, sending business borrowers hurrying to banks demanding credit at existing rates, and thereby forcing the Fed to supply additional reserves to the banking system. The additional reserves, in turn, will support more rapid money growth according to the editorial.

Third, the editorial suggests that the Federal Reserve's sole responsibility is to manage the money supply, which is taken to mean growth of the narrowly defined money supply, M-1. Further, the editorial seems to take a very short-run view of how closely the money stock should be controlled.

I am looking forward to reading your thoughts on these issues.

Sincerely,

William Proxmire
Chairman

Enc.
WP:srl

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

PAUL A. VOLCKER
CHAIRMAN

October 15

Dear Senator —

I appreciated the question on the membership issue this morning. It seems to me obvious that the kind of action we took does illustrate the problem and will increase the pressures. All I can say is that I feel a little helpless, "waiting and watching", at the moment!

Many thanks,

Paul

Senator Lugar

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

PAUL A. VOLCKER
CHAIRMAN

October 15, 1979

The Honorable Jim Mattox
House of Representatives
Washington, D.C. 20515

Dear Mr. Mattox:

Thank you for your letter of October 1, requesting the Board's views on your amendment to H.R. 2255 that would authorize bank holding companies to act as agent for the sale of property and casualty insurance to their subsidiaries.

As part of its implementation of the 1970 Amendments to the Bank Holding Company Act, the Board held an informal hearing on May 12, 1971 to consider the addition of certain insurance agency activities to the "laundry list" of permissible nonbanking activities pursuant to section 4(c)(8) of the Act. Numerous representatives of the insurance and banking industries testified at this hearing. On August 10, 1971, the Board announced its determination that certain insurance agency activities were so closely related to banking as to be a proper incident thereto. Among the types of insurance agency activities so authorized by the Board was the sale by bank holding companies of "any insurance for the holding company and its subsidiaries". 12 C.F.R. § 225.4(a)(9)(i).

Thereafter, the Board approved several applications by bank holding companies to sell insurance, including property and casualty for the holding company and its subsidiaries. In 1973, the Independent Insurance Agents of America ("IIAA") (formerly, the National Association of Insurance Agents) challenged the Board's approval of certain applications of bank holding companies to engage in insurance agency activities. Although these applications in part related to the sale of property and casualty insurance to the bank holding company, IIAA challenged only those portions of the application relating to the sale of property and casualty insurance to borrowers from the bank holding company system and did not challenge the sale of property and casualty insurance to the holding company and its subsidiaries. Formal hearings before an Administrative Law Judge were held regarding IIAA's protest to these applications. Upon the conclusion of the hearings, the Administrative Law Judge, among other things, recommended that bank holding companies be permitted to sell insurance for themselves and their subsidiaries. The Board approved (with certain modifications not relevant here) the recommended decision of the Administrative Law Judge.

The Honorable Jim Mattox
Page Two

In 1974, IIAA requested the United States Court of Appeals for the Fifth Circuit to review the Board's approval of these applications. Although IIAA did not contest the validity of the Board's approval relating to the sale by the bank holding companies of insurance for themselves and their subsidiaries, the Court on its own initiative invalidated the Board's finding that the sale of insurance for the bank holding company and the nonbanking subsidiaries is "closely related" to banking within the meaning of section 4(c)(8) of the Act. Alabama Association of Insurance Agents, Inc. v. Board of Governors, 533 F.2d 224 (5th Cir. 1976); rehearing denied, 558 F.2d 729 (5th Cir. 1977); cert. denied, 435 U.S. 904 (1978). The court, however, affirmed the Board's finding that the sale of insurance for the banking subsidiary of a bank holding company is closely related to banking.

Thus, the Board's 1971 conclusion that the sale of insurance for the bank holding company and its subsidiaries was an activity "closely related" to banking was affirmed in part and rejected in part by the Alabama court. Prior to the court's partial reversal of the Board's regulation, the Board found in its administration of the regulation that the sale of insurance, including property and casualty to the bank holding company and its subsidiaries, resulted in the lowering of overall insurance costs to the holding company system and, therefore, possible benefits to the public. Your proposed amendment to H.R. 2255 would restore the opportunity for bank holding companies to provide such benefits.

If we can be of any further assistance, please let us know.

Sincerely,

S/Paul A. Volcker

RW:smk (V-53)
bcc: Mr. Mannion
Mr. Bleier
Mr. Whiting
Mrs. Mallardi(2)

CONGRESS OF THE UNITED STATES
HOUSE OF REPRESENTATIVES

1979 OCT -2

October 1, 1979

JIM MATTOX
5TH DISTRICT, TEXAS

#53

Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Twentieth Street and
Constitution Avenue
Washington, D.C. 20551

Dear Mr. Chairman:

Enclosed is a copy of an amendment I offered during consideration of the bill H.R. 2255 by the House Committee on Banking, Subcommittee on Financial Institutions, Supervision, Regulation, and Insurance.

As you know, H.R. 2255 addresses the subject of the sale of insurance by bank holding companies.

This amendment has been the source of much discussion between myself, the bill's prime sponsor, Congressman Jim Hanley (D-NY), the Independent Insurance Agents of America, and those in bank holding companies whose insurance activities do not fall within the June 6, 1978 grandfather date. It would be of interest to all of these groups to have the opinion of the Federal Reserve when further negotiations commence in the second week in October. Therefore, I would appreciate it if your legal staff could provide us with some indication as to whether the Federal Reserve feels it would be wise to allow bank holding companies to continue to act as agent (only) in the sale of property and casualty insurance to their subsidiaries.

I am available to you and your legal division for any further information or discussion of this issue and look forward to receiving the Fed's opinion.

Sincerely,

Jim Mattox

Jim Mattox

JM:cb

Enclosure

WASHINGTON OFFICE: 1127 LONGWORTH HOUSE OFFICE BUILDING, WASHINGTON, D.C. 20515 (202) 225-2231
DISTRICT OFFICE: 5200 EAST GRAND AVENUE, SUITE 100, DALLAS, TEXAS 75223 (214) 767-2864

AMENDMENT TO BE OFFERED BY MR. MATTOX TO H.R. 2255

Page 2, line 9, after the word "or", insert a new subsection iii as follows:

> "(iii) any insurance agency activity where the insurance is limited to sales of fidelity and property and casualty insurance on the personnel and assets of a bank holding company or its subsidiaries, and group insurance that protects the bank holding company and its subsidiaries;"

Redesignate succeeding subsections accordingly.

Report language to accompany this amendment is suggested to read: "Nothing in this bill is meant to preclude Section 7 of the Bank Holding Company Act (12 U.S.C. Sec. 1846)".

October 15, 1979

The Honorable Harold S. Sawyer
Member of Congress
166 Federal Building
Grand Rapids, Michigan 49503

Dear Mr. Sawyer:

Thank you for your letter of October 2 on behalf of George D. Baldwin. Mr. Baldwin had encountered difficulty tracking down a transfer of funds through Federal Reserve facilities between Cleveland, Ohio, and Grand Rapids, Michigan.

Board staff has contacted the Federal Reserve Banks involved and have confirmed that Mr. Baldwin's transfer was sent by the Cleveland Trust Company on December 12, 1972, as indicated in your letter. It was acted on by the Cleveland Federal Reserve Bank and forwarded to the Detroit Office via our Culpeper, Virginia, facility within minutes of receiving it from Cleveland Trust. The Detroit Office only retains detailed records of transactions they have processed for 6 years, so that the records for December 1972 have already been destroyed. The records that are available for 1972 reflect only daily totals of debits and credits for each member bank, and not individual transactions. However, there is no record of any inquiry or unresolved discrepancies with the Michigan National Bank during this time period that would indicate any abnormality in handling this funds transfer.

We also investigated the comment regarding Mr. Baldwin's discussions with the Cleveland Federal Reserve Bank and their apparent lack of cooperation. Federal Reserve wire transfer operators in all offices are instructed to be cautious when providing information concerning funds transfers over the telephone, particularly when it involves names of individuals, account number, or dollar amounts. It is certainly not the Federal Reserve's intention to obstruct any efforts in tracking down transactions we have processed. However, we continue to strive to maintain high levels of security and privacy protection for all the transactions for which we are responsible, and part of that protection is not releasing detailed information to unknown individuals over the telephone. The normal procedure for this type of inquiry is for the individual to request his bank to work with the Federal Reserve to determine the disposition of the transaction.

The Honorable Harold S. Sawyer
Page Two

If the Federal Reserve can be of further assistance in this matter, Mr. Baldwin should feel free to contact either the Cleveland or Detroit Office directly or Mr. Richard Anstee, (202) 452-3927, at the Board of Governors in Washington.

Sincerely,

S/Paul A. Volcker

RPA:CO:pjt (#V-59)
bcc: Mr. Anstee
Mr. Wallace
Mrs. Mallardi (2)

HAROLD S. SAWYER
5TH DISTRICT, MICHIGAN

WASHINGTON OFFICE:
508 CANNON HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-3831

COMMITTEES:
JUDICIARY
VETERANS' AFFAIRS

SELECT COMMITTEES:
ASSASSINATIONS
ETHICS

Congress of the United States
House of Representatives
Washington, D.C. 20515

ADMINISTRATIVE ASSISTANT:
RUSSELL A. ROURKE

DISTRICT REPRESENTATIVE:
JOHN R. WESTMAN

DISTRICT OFFICE:
166 FEDERAL BUILDING
GRAND RAPIDS, MICHIGAN 49503
(616) 451-8383

October 2, 1979

#54

1979 OCT -5 PM 11:15

Mr. Paul A. Volcker
Chairman
Federal Reserve System
Twentieth Street and
Constitution Avenue NW
Washington, D.C. 20551

RE: George D. Baldwin

Dear Mr. Volcker:

I have been contacted by the above who has encountered some difficulty in tracking down a lost wire transfer between Cleveland, Ohio and Grand Rapids, Michigan.

The route of the wire transfer was to be as follows: from Cleveland Trust Company to Cleveland Federal Reserve; from Cleveland Federal Reserve to Detroit Federal Reserve; from Detroit Federal Reserve to Michigan National Bank in Grand Rapids.

The wire transfer, in the amount of [redacted] left Cleveland Trust Co. December 12, 1972 at 2:39 p.m., destination: Michigan National Bank account number [redacted].

Cleveland Federal Reserve will acknowledge only that they received the wire transfer from Cleveland Trust Company. They have told Mr. Baldwin that he must have a subpoena to obtain any further information regarding the progress of the wire transfer.

I cannot understand why the Cleveland Federal Reserve insists on impeding the progress on this search and request your assistance in tracking this down through Cleveland and Detroit as the transfer was never received by the bank in Grand Rapids.

PLEASE RESPOND TO: ☐ WASHINGTON OFFICE ☐ DISTRICT OFFICE

The timeliness of this matter is of the essence, as the statute of limitations on this expires in a little over a month.

Should the transfer be located, the money should be deposited in account number [redacted] at Grand Valley National Bank, Cascade Branch in Grand Rapids, as Mr. Baldwin has closed his account at Michigan National.

I look forward to hearing from you at your earliest convenience.

Yours very truly,

Hal Sawyer

Harold S. Sawyer
Member of Congress

HSS:kf
district office

#50

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

October 11, 1979

The Honorable Jacob K. Javits
United States Senate
Washington, D.C. 20510

Dear Jack:

Thank you for your letter of September 25 regarding U.S. policy on gold sales.

The recent rapid rise in the price of gold has been a disturbing development particularly as speculative interest in gold has spread to other commodities. These developments are symptomatic of the inflation problems all countries are facing. It is important for domestic reasons as well as to restore confidence in the dollar abroad that U.S. economic policy be directed toward improving our economic performance, particulary on inflation. This is the major objective of the Federal Reserve's actions announced on October 6. Other multilateral actions, such as the ones you mentioned in your letter, might also over time contribute to increased international monetary stability, but the principal responsibility for the dollar's international value lies with the United States.

The U.S. gold sales program has two main objectives. First, it is designed to reduce the U.S. trade deficit and to strengthen the balance of payments. In this respect the program is supportive of other efforts to maintain a sound and stable dollar. Second, the program is designed to contribute to the reduction of gold's role in the international monetary system--a goal that has been endorsed by most other countries.

The U.S. gold sales program has been successful. In 1978 we were a substantial net importer of gold; so far in 1979 we have recorded net exports of gold. Profits from the Treasury's gold sales have also contributed to the financing of the federal budget deficit. The program is accepted by the market and, in most cases, is welcomed by foreign monetary officials.

Although all possibilities should be carefully evaluated, I believe, under present circumstances, it would be unwise to suspend U.S. gold sales. Such an action would probably add further uncertainty to markets generally and contribute to increased speculation.

Sincerely,

Paul

Paul A. Volcker

JACOB K. JAVITS
NEW YORK

COMMITTEES:
FOREIGN RELATIONS
HUMAN RESOURCES
GOVERNMENTAL AFFAIRS
JOINT ECONOMIC

United States Senate

WASHINGTON, D.C. 20510

#50

REGIONAL OFFICES:
ROOM 511
110 EAST 45TH STREET
NEW YORK, NEW YORK 10017
ROOM 222
FEDERAL OFFICE BUILDING
111 WEST HURON STREET
BUFFALO, NEW YORK 14202
ROOM 420
LEO W. O'BRIEN FEDERAL BUILDING
CLINTON SQUARE
ALBANY, NEW YORK 12207

September 25, 1979

Dear Paul:

I would like to express my growing concern regarding our country's current policy of selling gold from our official gold stocks. Gold sales, initially intended to strengthen the international value of the dollar by absorbing excess dollars from the world market, now appear to be negating that objective by fueling a rush to buy gold, which is destabilizing the dollar market.

I believe that the present gold fever reflects a lack of confidence by investors in the world's currencies, including the traditional confidence in the dollar. Restoring confidence in the international monetary system will require in particular an improvement in the economic performance of the US, especially in the so-called fundamentals of inflation, energy, and the balance of payments. In addition, we must move quickly to deal with the structural problems facing the system by putting into place the Substitution Account in the IMF and improving national supervision and Central Bank regulation of the Eurocurrency markets.

These actions to stabilize the dollar will, however, not occur overnight, especially the Substitution Account, which will involve tough and sensitive negotiations with our trading partners and may require a more healthy international economic climate to be successful. In the immediate future, therefore, the question of whether or not the Treasury should continue to sell gold needs to be addressed. By my rough calculation, the loss to the US Treasury from gold sales since 1975 has been approximately 2 billion dollars; and, even as important as the dollar loss to the US Treasury is the fact that the other industrialized nations apparently do not share our objective of demonetizing gold; and, as a result, our gold sales may be exacerbating the present gold situation.

Therefore, it is a serious question whether we should not suspend our gold sales until the gold and other commodity markets have once again stabilized.

...n assigned to Division of Interr...tional
Finance

The Honorable Paul Volcker
Page 2
September 26, 1979

I will appreciate your considered attention to this matter, which is of the highest national interest, at your earliest convenience.

With best wishes,

Sincerely,

Jack

Jacob K. Javits, U.S.S.

The Honorable
Paul Volcker
Chairman
Board of Governors
Federal Reserve System
Federal Reserve Building
Room B1225
Washington, DC 20551

October 10, 1979

The Honorable Ralph Regula
House of Representatives
Washington, D.C. 20515

Dear Mr. Regula:

Thank you for your letter of October 9 recommending Mr. Robert Barone as a member of the Board's Consumer Advisory Council.

You may be assured that Mr. Barone's qualifications will receive full consideration by the Board when it makes the 1980 appointments to the Council within the next several weeks. We will be in touch with you when the selections are made.

The Board appreciates receiving your recommendation and your interest in the Consumer Advisory Council.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-63)
bcc: Anne Geary (w/copy of incoming)
Mrs. Mallardi (2)

RALPH REGULA
16TH DISTRICT, OHIO

CANNON HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-3876

DISTRICT OFFICES:
4150 BELDEN VILLAGE STREET NW.
CANTON, OHIO 44718
(216) 456-2869

201 EAST LIBERTY STREET
WOOSTER, OHIO 44691
(216) 264-3585

Congress of the United States
House of Representatives
Washington, D.C. 20515

COMMITTEES:
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SUBCOMMITTEES:
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MILITARY CONSTRUCTION
BUDGET
TASK FORCES:
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TAX POLICY
SELECT COMMITTEE ON AGING

October 9, 1979

#63

Honorable Paul Volcker, Chairman
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Mr. Chairman:

I understand that Robert Barone, Vice President and General Manager of the Diebold Company, has been nominated to the Consumer Advisory Council of the Federal Reserve Board.

Prior to joining Diebold, Mr. Barone worked for National Cash Register where he designed a comprehensive data system for the retailing industry. For the past eight years, Mr. Barone has worked for Diebold and has extensive experience with the automated teller machines.

The Diebold Company is the third largest manufacturer of automated teller machines. No other product has been as important to consumers in changing the patterns of traditional banking than the automated teller machine. It appears likely that the trend toward electronic consumer banking will increase in the years ahead.

I urge you to carefully consider Mr. Barone for a position on the Consumer Advisory Council.

Sincerely,

Ralph Regula, M.C.

R:Wc

October 10, 1979

The Honorable Alan Cranston
United States Senate
Washington, D. C. 20510

Dear Alan:

During our recent meeting in your office, I discussed the evolving position of some of the major trade associations on the Fed "membership" legislation and on my proposal for a supplemental reserve requirement on which interest would be paid.

The U. S. League has now come forward with their position on this proposal which the ABA had previously supported. I understand that Ken Guenther of my staff has already forwarded the formal ABA consensus statement to your staff. Enclosed is the position of the U. S. League and a summary of this position.

I find the support of these two major trade associations for a legislative solution encompassing a supplemental reserve requirement highly encouraging.

In my judgment the measures we announced this weekend make prompt legislative action more imperative since we have levied a new reserve tax on member banks. In turn, it is our considered judgment that Congressional passage of legislation providing for nationwide NOW accounts--which we support--will exacerbate our membership problem in the critical period ahead.

I appreciate your continued interest in this matter.

Sincerely,

S/Paul A. Volcker

Enclosure

KAG:vcd
bcc: Mrs. Mallardi (2)

October 10, 1979

The Honorable William L. Armstrong
United States Senate
Washington, D. C. 20510

Dear Senator Armstrong:

This is in response to the letter of October 4 sent jointly by Senator Garn and yourself, asking for the Board's assessment of whether or not the restitution provisions of S. 108 need to be amended in light of our experience with the Truth in Lending enforcement guidelines. As you observe in your letter, there are a number of differences between the provisions of S. 108 and the existing guidelines. More significant differences arise between S. 108 and the changes proposed to the guidelines endorsed by the Examination Council, which the Board today authorized to be published for public comment.

While the Board recognizes these differing provisions, it does not believe that changes to S. 108 are necessary. The Board notes that S. 108 becomes effective two years from the date of enactment. Thus, there should be ample opportunity in the ensuing two years for the banks subject to the Board's jurisdiction to develop compliance programs that eliminate patterns or practices resulting in violations involving reimbursements. We assume that S. 108 will address problems arising under fresh examinations conducted after the effective date of the legislation.

The Board appreciates the opportunity to comment on this matter. A substantively identical reply is being sent to Senator Garn.

Sincerely,

S/Paul A. Volcker

IDENTICAL LETTER TO SENATOR GARN

JCK:JPB:vcd (#V-55)
bcc: Mr. Kluckman
Mrs. Mallardi (2)

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, D.C. 20510

#55

October 4, 1979

The Honorable Paul A. Volcker
Chairman, Board of Governors of the
Federal Reserve System
Washington, D.C. 20037

Dear Mr. Chairman:

As a result of the five financial institution regulatory agencies' recent suspension of the Truth in Lending enforcement guidelines pending a reassessment of some of the basic provisions of those guidelines, we have become concerned about the restitution provisions in the Truth in Lending bill (S. 108) which passed the Senate in May. Since the suspension evidences a concern with proceeding under the current provisions of the guidelines and since the parameters for restitution contained in S. 108 are similar in many respects to those of the guidelines, we believe it is necessary to receive the views of the agencies on the restitution provisions contained in the Truth in Lending bill. We are interested in your assessment of the impact that the enactment of S. 108 would have upon the reimbursement policies and practices of the agencies and whether or not, in light of your experience, there is a need to amend the restitution section (section 8) of the Truth in Lending bill.

In assessing the need for amendments to the restitution provisions of the bill, we would appreciate it if you would take into account the following issues:

- Whether or not the problems encountered by the agencies under the guidelines and which resulted in the suspension of those guidelines would also be present if the agencies were operating under provisions of law as are contained in S. 108. Would the experience and problems be the same, similar or different? Would the scope of the problems which resulted in reconsideration of the guidelines be greater, lesser or the same if the agencies were operating under the specific provisions of S. 108?

• The agencies are presently considering changes in the enforcement guidelines with respect to the period for retroactive enforcement, the APR tolerance and flexibility of enforcement. What is the need for adjustments in these areas and if the present restitution provisions of S. 108 become law what latitude would the agencies believe they then have to make such adjustments?

• The agencies' guidelines presently provide for a number of exceptions to the general reimbursement rules. Is there a need for these exceptions and do you believe the agencies would have the latitude to provide for such exceptions under the provisions of S. 108? Please include an assessment of at least the following special provisions:

1. finance charge tolerance
2. special treatment for a total failure to disclose an APR
3. special treatment for certain violations involving credit life insurance
4. no reimbursement for a failure to comply with section 226.4(a)(6) disclosures involving property insurance
5. no reimbursement for a failure to itemize charges under section 226.4(b) of Regulation Z

(Note: presumably the violations listed in 3, 4 and 5 would all be finance charge violations and therefore subject to reimbursement under S. 108.)

Taking into account the above mentioned considerations, we would appreciate your assessment of the need for amendments to the Truth in Lending bill. Although your response will be very helpful in preparing for the hearings to be held by the Consumer Affairs Subcommittee, we are requesting a much earlier reply since the Truth in Lending provisions are part of the Financial Institution Deregulation bill which will be considered by the Senate very soon. Therefore, we would like to receive your reply by October 10, 1979.

Thank you for your prompt attention, as your views will be very important to our analysis of this issue.

Sincerely,

Bill Armstrong Jake Garn

William L. Armstrong Jake Garn

October 10, 1979

The Honorable Wes Watkins
House of Representatives
Washington, D.C. 20515

Dear Mr. Watkins:

Enclosed are Board staff responses to the specific questions posed in your letter to Chairman Volcker dated September 20, 1979, relating to the standards used by the Board in acting on one-bank holding company formations. As you will note, we do not maintain a data base on the actual numbers of cases where exceptions to the twelve year debt retirement period has been noted. The answers to some of the questions, therefore, are based on the experience and knowledge of Board and Reserve Bank staff.

I look forward to our meeting on Friday and welcome the opportunity to discuss this matter personally with you. If you or members of your staff wish further information or have any questions concerning the responses, please call John E. Ryan, Director of the Board's Division of Banking Supervision and Regulation (452-2893).

Sincerely,

/S/

Frederick H. Schultz

Enclosure

JER:pjt (#V-45)
bcc: Gov. Schultz
Jack Ryan
Mrs. Mallardi

October 9, 1979

The Honorable Bill Archer
House of Representatives
Washington, D. C. 20515

Dear Mr. Archer:

Thank you for your letter of September 27 recommending Mr. Robert T. Sakowitz as a member of the Board's Consumer Advisory Council.

You may be assured that Mr. Sakowitz' qualifications will receive full consideration by the Board when it makes the 1980 appointments to the Council this fall. We will be in touch with you when the selections are made.

The Board appreciates receiving your recommendation and your interest in the Consumer Advisory Council.

Sincerely,

S/Paul A. Volcker

CO:vcd (#V-60)

bcc: Mrs. Mallardi (2)
Anne Geary (w/copy of incoming)

BILL ARCHER
7TH DISTRICT, TEXAS

MEMBER:
WAYS AND MEANS
COMMITTEE

Congress of the United States
House of Representatives
Washington, D.C. 20515

WASHINGTON OFFICE:
LONGWORTH
HOUSE OFFICE BUILDING

DISTRICT OFFICE:
FEDERAL OFFICE BUILDING
HOUSTON, TEXAS 77002

1979 OCT -5 ... 11:15

#60

September 27, 1979

Dear Mr. Chairman:

It is my understanding that the Board of Governors of the Federal Reserve System is currently searching for qualified individuals to serve on the Consumer Advisory Council. I would like to take this opportunity to acquaint you with a person I believe is eminently qualified for this appointment, Mr. Robert T. Sakowitz.

Bob Sakowitz is president of Sakowitz, Inc., a very distinguished specialty department store chain based in Houston, Texas. It has been my great pleasure and privilege to know Bob for many years. Not only has he reached the pinnacle of the retailing profession, he has notably distinguished himself in the many public service endeavors he has undertaken. I am convinced that Bob will make many strong contributions in this capacity both to the consumers of our nation, the federal government and the retailing industry. In my opinion, there is no finer person than Bob Sakowitz for this important position and I give him my highest recommendation.

Thank you very much for your consideration of Robert Sakowitz and with best wishes, I am

Sincerely,

Bill Archer

Bill Archer, M.C.

Honorable Paul A. Volcker
Chairman
Federal Reserve System
20th Street and Constitution Avenue, N. W.
Washington, D. C. 20551

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October 9, 1979

The Honorable Paul E. Tsongas
Chairman
Subcommittee on Consumer Affairs
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Tsongas:

Thank you for your letter of October 4 regarding the change in the schedule for your Subcommittee's hearings on the review of Truth in Lending enforcement policies.

Governor Nancy H. Teeters will be pleased to appear on behalf of the Board on October 31.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-56)
bcc: Gov. Teeters (w/copy of incoming)
Janet Hart " " "
Mrs. Mallardi (2)

United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, D.C. 20510

October 4, 1979

#56

The Honorable Paul A. Volcker
Chairman
Board of Governors of the
Federal Reserve System
Washington, D.C. 20037

Dear Chairman,

I wish to advise you that the hearings by the Consumer Affairs Subcommittee, originally scheduled for October 16th and 17th, have been rescheduled for October 31st and November 1st, 1979.

I wish to extend to you an invitation to testify on the morning of October 31st. The hearings will be held in the Senate Banking Committee hearing room.

Thank you for your cooperation.

Sincerely,

Paul Tsongas

Paul E. Tsongas, Chairman
Consumer Affairs Subcommittee

Enclosure

United States Senate
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, D.C. 20510

GUIDELINES FOR WITNESSES

1. These guidelines apply to all hearings of the Senate Committee on Banking, Housing and Urban Affairs, unless otherwise indicated.

2. All hearings will begin at 10:00 A.M. in Room 5302, Dirksen Office Building, unless otherwise indicated.

3. Committee rules require that all witnesses submit at least 100 copies of their written statements 48 hours prior to their appearance. Sundays and holidays are not to be included in determining this 48-hour period. Statements should be delivered to Room 5300, Dirksen Office Building, Washington, D. C. 20510. Strict adherence to this rule is essential in order that Committee members may review the statements before the hearing, thus enabling the participants to more thoroughly discuss the issues involved. Statements will not be released to the news media prior to the day of your testimony.

4. Oral presentations must be limited to a brief summary not to exceed 10 minutes. Your complete statement will be printed in the hearing record.

5. Please complete the attached card and bring it to Room 5300 prior to the hearing. You will be given copies of statements of those testifying with you at that time.

ion is appreciated.

Please supply the address to which you prefer the reporter's transcript delivered for your correction.
Kindly turn this card in at Room 5300 Dirksen Office Building prior to giving your testimony.

(Name)

(Organization)

(Business address) (Phone)

(City and State) (ZIP Code)

SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE

36-545-h GPO

OCT 9 1979

The Honorable Walter F. Mondale
President of the United States Senate
Washington, D.C. 20510

Dear Mr. Vice President:

As required by § 904(a)(4) of the Electronic Fund Transfer Act, Public Law 95-630, the Board of Governors is pleased to submit to the Congress the enclosed proposed regulation.

The Board has adopted portions of Regulation E to implement the Electronic Fund Transfer Act, and is republishing for public comment other sections of the regulation. The enclosed documents include the final and proposed regulations and their accompanying economic impact analyses.

Sincerely,

S/Paul A. Volcker

Enclosures
LBB:DJW:pjt
bcc: Lynne Barrx
Mrs. Mallardi (2)

Identical ltrs. sent to:
Speaker O'Neill; Chairmen Tsongas, Proxmire, Reuss, Annunzio; Senators Garn and Armstrong; Cong. Stanton and Whlie.

October 5, 1979

The Honorable George Hansen
House of Representatives
Washington, D.C. 20515

Dear Mr. Hansen:

I am pleased to respond to your recent request for the views of the Board of Governors concerning your proposed amendment to H.R. 5037, which would affect the term of the Federal Reserve Chairman. The amendment that you have proposed is intended to assure the President a wide choice in the appointment of the Chairman, without regard to the geographic restrictions that are currently contained in the Federal Reserve Act.

The Board believes that it is advisable to provide the President flexibility in selecting a Federal Reserve Chairman. Because of the significant responsibilities that the Federal Reserve Act places on the Chairman, the Board agrees that the President should be permitted to select the best available person for the position and should not be limited by geographic constraints in the selection. The Board, therefore, supports an amendment to the Federal Reserve Act that would permit the President to name a Chairman without regard to whether the Federal Reserve district from which the Chairman is appointed already is represented on the Board.

The Board is concerned, however, about a possible technical defect in the draft language of the proposed amendment. This amendment would appear to require that at least five Federal Reserve districts be represented on the Board at all times. This requirement could present difficulties if there were several vacancies on the Board at a particular time, as was the case during the past year. For example, if there were two vacancies on the Board and the Chairman and one other member were from the same district, only four districts would be represented on the Board, contrary to the requirement that five districts be represented.

The Honorable George Hansen
Page Two

Therefore, in order to accomplish your objective, the Board proposes that the first paragraph of section 10 of the Act (12 U.S.C. § 241) be amended by adding the underlined language:

> "In selecting the members of the Board, not more than one of whom shall be selected from any one Federal Reserve district, <u>except that two members may represent the same district if one is serving as Chairman or has served as Chairman</u>, the President shall have due regard to a fair representation of the financial, agricultural, industrial, and commercial interests, and geographical divisions of the country."

Sincerely,

S/Paul A. Volcker

LSA:smk (#V-41)
bcc: Mr. Petersen
Mr. Adams
Mrs. Mallardi(2)

A[illegible]ion assigned Mr. Petersen

U.S. HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON DOMESTIC MONETARY POLICY
OF THE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SIXTH CONGRESS
WASHINGTON, D.C. 20515

#41

1979 SEP 20 PM 10:47

September 19, 1979

The Honorable Paul Volcker, Chairman
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Mr. Volcker:

It is my intention to offer the enclosed amendment to the bill H.R. 5037, regarding the term of the Federal Reserve Chairman, when that bill is marked up by the Committee on Banking, Finance and Urban Affairs.

The intent of the amendment is to assure the President a wide choice in his appointment of a Chairman, without regard to a geographic constraint that is not properly relevant to an office of completely national significance and responsibility. At the same time, I have, in consultation with other Members of the Subcommittee on Domestic Monetary Policy, worked out the language of the amendment so that there is still a guarantee of diversified regional outlooks on the Board of Governors.

I can imagine in the future a situation in which the obviously right choice for Chairman is obviously not from an "open" district, and the Board of Governors and Open Market Committee might be subject to a nuisance suit challenging the legality of the appointment and the validity of votes taken, and so on. It is to prevent such a thing that I believe we ought to take this opportunity to adopt this amendment.

I would greatly appreciate having the comments of the Board on this amendment.

Yours for individual liberty,

George Hansen

George Hansen, M.C.

GH:lcg

Amendment Offered to H.R. ~~4997~~ 5037

by Mr. Hansen

Add the following new section:

Sec. 3 (a) The second sentence of the first paragraph of section 10 of the Federal Reserve Act (12 U.S.C. 241) is amended by striking out the phrase "not more than one of whom shall be selected from any one Federal Reserve District,".

(b) Insert the following new sentences immediately after the second sentence of the first paragraph of Section 10 of the Federal Reserve Act:

"Not fewer than five Federal Reserve districts shall be represented at any one time and a particular district may be represented by two members only if one is designated to serve as Chairman or has served as Chairman of the Board."

CM

OCT 4 1979

The Honorable Paul E. Tsongas
Chairman
Subcommittee on Consumer Affairs
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Chairman Tsongas:

Thank you for your letter of September 14 inviting the Board to testify before your Subcommittee at hearings to review the Truth-In-Lending enforcement policies of the federal regulatory authorities.

The Board will be unable to testify at the hearing to be held on October 16 because the Federal Open Market Committee is scheduled to meet on that day. However, Governor Nancy H. Teeters will be pleased to appear on behalf of the Board on October 17.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-44)
bcc: Gov. Teeters
Janet Hart (w/copy of incoming)

#44

United States Senate

COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS

WASHINGTON, D.C. 20510

September 14, 1979

The Honorable Paul A. Volcker
Chairman, Board of Governors of the
Federal Reserve System
Washington, D.C. 20037

Dear Chairman,

We have scheduled hearings on October 16th and 17th by the Consumer Affairs Subcommittee of the Senate Banking Committee to review the Truth-In-Lending enforcement policies of the federal regulatory authorities.

I believe the testimony of a representative of the Federal Reserve Board would be very helpful to the deliberations of the subcommittee. On behalf of the Subcommittee, I wish to extend to the Federal Reserve Board an invitation to testify on the morning of October 16th. The hearings will be held in the Senate Banking Committee hearing room.

Thank you for your cooperation.

Sincerely,

Paul

Paul E. Tsongas, Chairman
Consumer Affairs Subcommittee

October 3, 1979

The Honorable Thomas A. Luken
House of Representatives
Washington, D.C. 20515

Dear Mr. Luken:

Thank you for your letter of September 27 recommending Mr. Joseph M. Garber as a member of the Board's Consumer Advisory Council.

You may be assured that Mr. Garber's qualifications will receive full consideration by the Board when it makes the 1980 appointments to the Council this fall. We will be in touch with you when the selections are made.

The Board appreciates receiving your recommendation and your interest in the Consumer Advisory Council.

Sincerely,

S/Paul A. Volcker

CO:pjt (#V-52)
bcc: Anne Geary (w/copy of incoming)
Mrs. Mallardi (2)

THOMAS A. LUKEN
2D DISTRICT, OHIO

WASHINGTON OFFICE:
ROOM 1131
LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-2216

DISTRICT OFFICES:
3409 FEDERAL OFFICE BUILDING
CINCINNATI, OHIO 45202
(513) 684-2723

MOBILE OFFICE

Congress of the United States
House of Representatives
Washington, D.C. 20515

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SUBCOMMITTEE ON COMMUNICATIONS
SUBCOMMITTEE ON CONSUMER PROTECTION AND FINANCE
SELECT COMMITTEE ON AGING
SUBCOMMITTEE ON HEALTH AND LONG TERM CARE

#52

1979 OCT -2 PM 2:36

September 27, 1979

Mr. Paul A. Volcker
Board of Governors of the Federal Reserve System
Federal Reserve Building
20 Constitution Avenue N.W.
Washington, D.C. 20551

Dear Mr. Volcker:

I am writing to endorse the appointment of Joseph M. Garber to a position on the Consumer Advisory Council of the Federal Reserve Board. Mr. Garber's credentials for such an appointment are impeccable.

As President of the Credit Bureau of Cincinnati, Inc. and First Vice President of the Board of Associated Credit Bureaus, Joe Garber would be as asset to the Board both as an adviser on the creditors prospective on issues which come before the Board, as well as a consultant on compliance with the terms of the Consumer Credit Protection Act. Joe has devoted his life to the credit industry both as an academic and a practicioner. He has achieved industry and civic stature through his work, not only in the Midwest but on a national basis.

The Board would be well advise to give him their most serious consideration. I would appreciate being kept advised on your deliberations on this matter and hope that you see the wisdom of adding Joe Garber to the Consumer Advisory Council.

Thanking you in advance for your consideration in this matter.

Sincerely,

Thomas A. Luken

THOMAS A. LUKEN
Member-of-Congress

TAL/mjb

October 3, 1979

The Honorable Dale Evans
House of Representatives
Washington, D.C. 20515

Dear Mr. Evans:

Thank you for your letter of September 27 requesting my comments on legislation that would extend for two additional years the December 31, 1980 divestiture deadline in the Bank Holding Company Act for companies required to divest certain real estate interests. In considering this issue, I found that last year the Board addressed a similar proposal and expressed its concern that such a proposal could reopen the general question of the December 31, 1980 deadline and might be inequitable to those companies that had complied with that deadline.

While I have not had the opportunity to consult with the full Board, I can well recognize the nature of their earlier concerns, and I am sure you would want to take these concerns into account. I am not in a position at this time to evaluate the hardships imposed on individual holding companies in meeting the statutory deadline. Nevertheless, in response to a similar inquiry by members of the Senate Banking Committee, I suggested as a possible approach a limited two-year extension of the December 31, 1980 deadline. The extension would be granted by the Board only if the Board determined there was a compelling case presented for an extension and that good faith efforts had been made to meet the existing statutory deadline. It is my understanding that the Senate Banking Committee on September 24 adopted such a provision as an amendment to S. 1347.

I appreciate the opportunity you have afforded me to comment on this proposal.

Sincerely,

S/Paul A. Volcker

(MLP:REM:MEB:)DJW:pjt (#V-48)
bcc: Mike Bleier
Mrs. Mallardi (2)

BANKING, FINANCE AND URBAN AFFAIRS COMMITTEE

GOVERNMENT OPERATIONS COMMITTEE

SELECT COMMITTEE ON AGING

STEERING COMMITTEE: MIDWEST-NORTHEAST ECONOMIC ADVANCEMENT COALITION

Congress of the United States
House of Representatives
Washington, D.C. 20515

DAVE EVANS
6TH DISTRICT, INDIANA

DISTRICT OFFICE:
4TH FLOOR ADMINISTRATION BUILDING
INDIANAPOLIS INTERNATIONAL AIRPORT
INDIANAPOLIS, INDIANA 46241
TELEPHONE: (317) 269-7364
TOLL FREE NUMBER:
OPERATOR-ENTERPRISE 7364

WASHINGTON OFFICE:
438 CANNON OFFICE BUILDING
WASHINGTON, D.C. 20515
TELEPHONE: (202) 225-2276

#48

1979 SEP 28 AM 11:23

September 27, 1979

The Honorable Paul A. Volcker
Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

Dear Chairman Volcker:

I am writing to inquire as to the Fed's position on proposed legislation that would extend the present divestiture deadline in the Bank Holding Company Act.

As you know, Section 4 of the Bank Holding Company Act of 1970 required bank holding companies to divest themselves of non-banking related interests by December 31, 1980. Prior to the 1970 law, a number of bank holding companies lawfully acquired interests in real estate for investment or development. While the ten-year period was considered by Congress to be ample time, a severe real estate recession has intervened during this period and has made the task of timely divestiture of real estate holdings exceedingly difficult.

The House Banking Committee may shortly consider an amendment which would extend the divestiture period for real estate interests until December 31, 1982. I understand that the application of this provision would be limited to relatively few instances where the holding companies would have to sell properties at prices substantially below fair value owing to the approach of the current deadline.

The extension is strictly limited to real estate interests, and cannot be used for further development. Because of the unique impact of the recession on real estate, I do not believe the extension could be viewed as a precedent for extending the divestiture period for any other activities not "closely related" to banking.

Sincerely,

Dave Evans

DAVE EVANS
Member of Congress

DE:gk

October 3, 1979

The Honorable Parren J. Mitchell
Chairman
Subcommittee on Domestic Monetary Policy
Committee on Banking, Finance and Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Chairman Mitchell:

You have asked for my views on H.R. 5037, the bill to establish a fixed four-year term for the Chairman of the Federal Reserve that would expire on January 31 of the calendar year following the year during which a newly elected President is inaugurated. In the circumstances, I thought it appropriate to consult with my colleagues on the Board.

In our discussion, concern was expressed over the problem of a "short term" that would be created whenever a Chairman resigned, died or otherwise left office before his four-year fixed term expired. In such circumstances, under the bill a new Chairman would be appointed to serve only the remainder of the term. If the time period were short, qualified individuals might be reluctant to accept appointment, or the actions of an appointee might be constrained by the need for early reappointment.

As we discussed, the problem would be partially remedied if the bill were amended so that the President could appoint a Chairman to an expanded term in the event that a vacancy occurs during the last year of the fixed term. A recently elected President would then appoint a new Chairman to a term of up to five years (the remaining months of an unexpired term plus a full four-year term) in the event of a vacancy at the time of his inauguration or during the first year of his term.

No really adequate legislative solution for the problem of a vacancy late in a Presidential term of office--possibly in the heat of a political campaign--seems possible. However, similar contingencies could arise under existing legislation.

Your letter of September 28 states that you plan to offer two amendments to the legislation. One amendment would provide for the circumstance described above, that is, when a vacancy occurs within the last year of an unexpired term. The second amendment provides that the legislation would not affect the length of the term of the Chairman who is holding office at the time the bill is enacted.

After considering the "short term" problem and the amendments you propose, the Board does not believe the proposal would impair the essential independence of the Federal Reserve and supports the enactment of a bill with the amendments you plan to offer.

Sincerely,

S/ Paul

DJW:PAV:pjt (#V-51)
bcc: Mrs. Mallardi (2)

PARREN J. MITCHELL, MD., CHAIRMAN

STEPHEN L. NEAL, N.C.
NORMAN E. D'AMOURS, N.H.
DOUG BARNARD, GA.
JIM MATTOX, TEX.
JOHN J. CAVANAUGH, NEBR.

225-7315

GEORGE HANSEN IDAHO
RON PAUL, TEX.
DON RITTER, PA.

U.S. HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON DOMESTIC MONETARY POLICY
OF THE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SIXTH CONGRESS
WASHINGTON, D.C. 20515

September 28, 1979 #51

Mike Bleier in Legal Division will be handling.

The Honorable Paul A. Volcker
Chairman, Board of Governors
Federal Reserve System
20th and Constitution Avenue N.W.
Washington, D.C. 20551

Dear Mr. Chairman:

Enclosed is a copy of H.R. 5037, a bill to provide for a four-year term for the Chairman of the Federal Reserve Board to begin on January 31 of the year after a newly elected President takes office. Unexpired portions of the term would be filled for only the unexpired portion. This bill is identical to H.R. 4997 which the Subcommittee favorably reported by a vote of six ayes to zero nays on July 24, 1979. It is my hope that the full Committee will consider this legislation shortly after the October district work period ends.

I plan to introduce two amendments when the Committee marks up H.R. 5037. The first would provide for appointment of a Chairman to both a full four-year term and the unexpired portion of a term if the unexpired portion were less than one year. The second would amend Section 2 of H.R. 5037 so that "any person who is the Chairman of the Board of Governors of the Federal Reserve System immediately prior to the date of enactment of this Act may continue in the office of Chairman until the expiration of the four-year term for which he was appointed and the immediately following term shall expire on the next January 31 of the first calendar year commencing after the calendar year during which a Presidential term is scheduled to expire."

The first of the above amendments provides that in the event a Chairman resigns or dies within one year of the scheduled expiration of his term as Chairman, a President will be able to assure his replacement that he will serve as Chairman for more than one year. The second makes certain that the legislation, as I originally intended, will not reduce the term of whoever is serving as Chairman when the bill is enacted.

I would like to have your opinion and that of the Board on the bill to present to the full Committee when we take up H.R. 5037, hence I am hopeful that you will forward in writing your opinion and that of the Board as soon as possible.

Sincerely,

Parren J. Mitchell

Parren J. Mitchell, M.C.
Chairman

PJM/rwjt
enclosure

I

96TH CONGRESS
1ST SESSION

H. R. 5037

To amend the Federal Reserve Act respecting the positions of chairman and vice chairman of the Federal Reserve Board.

IN THE HOUSE OF REPRESENTATIVES

JULY 31, 1979

Mr. MITCHELL of Maryland (for himself, Mr. D'AMOURS, Mr. BARNARD, Mr. MATTOX, and Mr. CAVANAUGH) introduced the following bill; which was referred to the Committee on Banking, Finance and Urban Affairs

---

A BILL

To amend the Federal Reserve Act respecting the positions of chairman and vice chairman of the Federal Reserve Board.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) the second paragraph of section 10 of the Federal Reserve Act (12 U.S.C. 242) is amended by striking out the third sentence and inserting in lieu thereof the following: "The President shall appoint, by and with the advice and consent of the Senate, one member of the Board to serve as chairman. The chairman's term shall expire on January 31 of the first calendar year beginning after the calendar year during which the term of the President appointing him is scheduled to expire. In the event a chairman does not complete his entire term, his successor shall be appointed to complete the unexpired portion of such term. The President also shall appoint, by and with the advice and consent of the Senate, one member of the Board to serve as vice chairman for a term of four years.".

(b) The second paragraph of section 10 of the Federal Reserve Act (12 U.S.C. 242) is amended by inserting the following before the sentence which prior to the amendment made by subsection (a) of this section was the fourth sentence of such paragraph: "In the event of the unavailability of the chairman or a vacancy in the office of the chairman, the vice chairman shall have the power to act as chairman during such unavailability or, in the event of a vacancy, pending the appointment and qualification of such chairman's successor. Upon the expiration of the term of the office of the chairman or vice chairman, the chairman or vice chairman, as the case may be, shall continue to serve in such capacity until his successor is appointed and has qualified.".

SEC. 2. The amendments made by the first section of this Act shall take effect on the date of the enactment of this Act, except that the term, as chairman, of any person who is serving as chairman on January 31, 1982, shall expire on such date.

Don Wir handling

October 3, 1979

The Honorable Fernand J. St Germain
Chairman
Subcommittee on Financial Institutions
Supervision, Regulation and Insurance
Committee on Banking, Finance and
Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Chairman St Germain:

Thank you for your letter of October 1 inviting the Board to testify at your Subcommittee's hearing on a number of pending bank holding company bills and legislation permitting banks to underwrite revenue bonds.

Governor J. Charles Partee will be pleased to appear on behalf of the Board at 10:00 a.m. on October 17.

Sincerely,

S/ Paul

CO:pjt (#V-54
bcc: Gov. Partee
Mr. Kichline
Mr. Eisenbeis
Mr. Mannion (w/copy of incoming, w/o bills)

Mrs. Mallardi (2)

October 2, 1979

The Honorable Jacob K. Javits
United States Senate
Washington, D. C. 20510

Dear Senator Javits:

In Chairman Volcker's absence, I want to acknowledge receipt of your letter of September 25 regarding the Treasury's sale of gold from the U. S. gold stock. Your letter will be called to the Chairman's attention when he returns, and I am sure you will be hearing from him in the near future.

Sincerely,

/S/

Frederick H. Schultz

CO:DJW:vcd (#V-30)

bcc: Gov. Schultz
Mr. Siegman
Mr. Don Adams
Mrs. Mallardi (2)