

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

March 22, 1983

## CONFIDENTIAL (FR)

TO: Federal Open Market Committee

FROM: Normand Bernard W.B.

Attached is a staff recommendation to delete references in various Committee instruments to the authority for making direct loans of up to \$5 billion to the U.S. Treasury. This matter is listed as Item 6B on the agenda for next week's meeting.

Attachment

March 22, 1983

TO: Federal Open Market

SUBJECT: FOMC Instruments Relating

Committee

to Direct Lending to Treasury

FROM: Normand Bernard (5)

Agenda item 6B for the upcoming meeting contemplates amending three FOMC instruments by deleting references in them to the expired authority for direct lending to the U.S. Treasury. The instruments in question are (1) paragraph 2 of the Authorization for Domestic Open Market Operations, (2) paragraph 2 of the Resolution of Federal Open Market Committee Authorizing Certain Actions by Federal Reserve Banks During an Emergency, and (3) section 270.4(d) of the Regulation Relating to Open Market Operations of Federal Reserve Banks.

#### Discussion

The System's authority to lend up to \$5 billion directly to the U.S. Treasury dates from March 1942. In the past, Congress has enacted this legislation for limited periods and has occasionally allowed it to lapse prior to its renewal. The most recent renewal was approved on June 8, 1979 for a two-year period ending June 8, 1981. Since the latter date, therefore, the FOMC lending authorization has been in de facto suspension. Prior to June 8, 1979, the authorization had been in de facto suspension on several occasions, as the appended table illustrates, but the germane FOMC instruments were left in place on the expectation that the legislation would eventually be reenacted. Currently, the Board's legislative liaison staff are not aware

of any moves in the Congress or at the Treasury to renew the legislation. The last Treasury effort in that direction was a letter sent by Deputy Secretary McNamar in May 1981 to the U.S. Senate urging a 5-year extension of the authority, albeit without the complicated approval procedures contained in the June 8, 1979 legislation.1/

In light of the <u>de facto</u> suspension of the direct lending authority and the apparent absence of efforts to secure new legislation, the staff recommends that the Committee delete paragraph 2 from the current Authorization for Domestic Open Market Operations, and make conforming amendments in the other FOMC instruments cited above. Copies of the instruments indicating the recommended deletions are attached.

Attachments

I/ Public Law 96-18, approved June 8, 1979 for a two-year period, provided that Federal Reserve Banks might purchase U.S. obligations directly from the Treasury only in unusual and exigent circumstances for renewable periods not to exceed 30 days; these purchases could be made only when authorized by an affirmative vote of not less than five members of the Board of Governors. In other circumstances, The Treasury Department was authorized to borrow securities from the Federal Reserve and to sell them in the open market for the purpose of meeting its short-term cash needs. The Treasury was required to purchase these securities and return them to the Federal Reserve not more than six months after the date of sale. Earlier, less complex legislation had permitted the FOMC to authorize up to \$5 billion in direct loans to the Treasury.

## Periods of <u>de facto</u> Suspension of Direct Lending Authority

Dates	Length of Suspension
Since 6/9/81	21 months
5/2/79 to 6/7/79	36 days
5/1/78 to 10/26/78	179 days
10/1/77 to 11/6/77	37 days
11/2/76 to 4/18/77	168 days
11/1/75 to 11/11/75	10 days

#### AUTHORIZATION FOR DOMESTIC OPEN MARKET OPERATIONS

- 1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the most recent domestic policy directive adopted at a meeting of the Committee:
- (a) To buy or sell U. S. Government securities, including securities of the Federal Financing Bank, and securities that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States in the open market, from or to securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices, and, for such Account, to exchange maturing U. S. Government and Federal agency securities with the Treasury or the individual agencies or to allow them to mature without replacement; provided that the aggregate amount of U. S. Government and Federal agency securities held in such Account (including forward commitments) at the close of business on the day of a meeting of the Committee at which action is taken with respect to a domestic policy directive shall not be increased or decreased by more than \$3.0 billion during the period commencing with the opening of business on the day following such meeting and ending with the close of business on the day of the next such meeting;
- (b) When appropriate, to buy or sell in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates, prime bankers acceptances with maturities of up to nine months at the time of acceptance that (1) arise out of the current shipment of goods between countries or within the United States, or (2) arise out of the storage within the United States of goods under contract of sale or expected to move into the channels of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods; provided that the aggregate amount of bankers acceptances held at any one time shall not exceed \$100 million;
- (c) To buy U. S. Government securities, obligations that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, and prime bankers acceptances of the types authorized for purchase under 1(b) above, from dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities, obligations, or acceptances in 15 calendar days or less, at rates that, unless otherwise expressly authorized by the Committee, shall be determined by competitive bidding, after applying reasonable

limitations on the volume of agreements with individual dealers; provided that in the event Government securities or agency issues covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2 - - The -Federal -Open -Market -Committee -authorizes -and -directs -the -Federal Reserve -Bank -of -New-York - (or; -under -special -circumstances; -such -as -when -the New-York-Reserve-Bank-is-closed; -any-other-Federal-Reserve-Bank)-(a)-to lend-to-the-Treasury-such-amounts-of-securities-held-in-the-System-Open Market -Aecount -as -may -be -necessary -from -time -to -time -for -the -temporary accommodation -of-the-Treasury; -under-such -conditions -as-the-Gommittee-may specify: -and-(b)-to-purchase-directly-from-the-Treasury-for-renewable periods -not -to -exceed -thirty -days; -when -authorized -by -the -Board -of Governors -of -the -Federal -Reserve -System -pursuant -to -an -affirmative -vote -of not -less -than -five -members; -for -its -own -account -(with -discretion; -in -cases where -it -seems -desirable; -to -issue -participations -to -one -or -more -Federal Reserve -Banks) -such -amounts -of -special -short-term -certificates -of -indebtedness -as -may -be -necessary -from -time -to -time -for -the -temporary -accommodation of -the -Treasury; -provided -that -the -rate -charged -on -such -certificates -shall be-a-rate-of-1/4-of-1-percent-below-the-discount-rate-of-the-Federal-Reserve Bank -of -New -York -at -the -time -of -such -purchases -and -provided -that -the -total amount -of -such -certificates -held -at -any -one -time -by -the -Federal -Reserve Banks -shall -not -exceed -\$2 -billion:

- 2. 3. In order to ensure the effective conduct of open market operations, the Federal Open Market Committee authorizes and directs the Federal Reserve Banks to lend U. S. Government securities held in the System Open Market Account to Government securities dealers and to banks participating in Government securities clearing arrangements conducted through a Federal Reserve Bank, under such instructions as the Committee may specify from time to time.
- 3. 4. In order to ensure the effective conduct of open market operations, while assisting in the provision of short-term investments for foreign and international accounts maintained at the Federal Reserve Bank of New York, the Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York (a) for System Open Market Account, to sell U. S. Government securities to such foreign and international accounts on the bases set forth in paragraph 1(a) under agreements providing for the resale by such accounts of those securities within 15 calendar days on terms comparable to those available on such transactions in the market; and (b) for New York Bank account, when appropriate, to undertake with dealers, subject to the conditions imposed on purchases and sales of securities in paragraph 1(c), repurchase agreements in U. S. Government and agency securities, and to arrange corresponding sale and repurchase agreements between its own account and foreign and international accounts maintained at the Bank. Transactions undertaken with such accounts under the provisions of this paragraph may provide for a service fee when appropriate.

## RESOLUTION OF FEDERAL OPEN MARKET COMMITTEE AUTHORIZING CERTAIN ACTIONS BY FEDERAL RESERVE BANKS DURING AN EMERGENCY

The Federal Open Market Committee hereby authorizes each Federal Reserve Bank to take any or all of the actions set forth below during war or defense emergency when such Federal Reserve Bank finds itself unable after reasonable efforts to be in communication with the Federal Open Market Committee (or with the Interim Committee acting in lieu of the Federal Open Market Committee) or when the Federal Open Market Committee (or such Interim Committee) is unable to function.

- (1) Whenever it deems it necessary in the light of economic conditions and the general credit situation then prevailing (after taking into account the possibility of providing necessary credit through advances secured by direct obligations of the United States under the last paragraph of section 13 of the Federal Reserve Act), such Federal Reserve Bank may purchase and sell obligations of the United States for its own account, either outright or under repurchase agreement, from and to banks, dealers or other holders of such obligations.
- (2) Such Federal Reserve Bank may in its discretion purchase special cortificates of indebtedness directly from the United States in such amounts as may be needed to cover over-drafts in the general account of the Treasurer of the United States on the books of such Bank or for the temporary accommodation of the Treasury, but such Bank shall take all steps practicable at the time to insure as far as possible that the amount of obligations acquired directly from the United States and held by it, together with the amount of such obligations so acquired and held by all other Federal Reserve Banks, does not exceed \$5 billion at any one time.
- (2) (3) Such Federal Reserve Bank may engage in operations of the types specified in the Committee's authorization for System foreign currency operations when requested to do so by an authorized official of the U.S. Treasury Department; provided, however, that such Bank shall take all steps practicable at the time to insure as far as possible that, in light of the information available on other System foreign currency operations, its own operations do not result in the aggregate in breaching any of the several dollar limits specified in the authorization.

Authority to take the actions set forth shall be effective only until such time as the Federal Reserve Bank is able again to establish communications with the Federal Open Market Committee (or the Interim Committee), and such Committee is then functioning.

#### REGULATION RELATING TO OPEN MARKET OPERATIONS OF FEDERAL RESERVE BANKS

#### SECTION '270.1---AUTHORITY

This Part is issued by the Federal Open Market Committee (the "Committee") pursuant to authority conferred upon it by sections 12A and 14 of the Federal Reserve Act (12 U.S.C. § § 263, 355).

#### SECTION 270.2—DEFINITIONS

- (a) The term "obligations" means Government securities, U. S. agency securities, bankers' acceptances, bills of exchange, cable transfers, bonds, notes, warrants, debentures, and other obligations that Federal Reserve Banks are authorized by law to purchase and sell.
- (b) The term "Government securities" means direct obligations of the United States (i.e., U. S. bonds, notes, certificates of indebtedness, and Treasury bills) and obligations fully guaranteed as to principal and interest by the United States.
- (c) The term "U. S. agency securities" means obligations that are direct obligations of, or are fully guaranteed as to principal and interest by, any agency of the United States.
- (d) The term "System Open Market Account" means the obligations acquired pursuant to authorizations and directives issued by the Committee and held on behalf of all Federal Reserve Banks.

#### SECTION 270.3—GOVERNING PRINCIPLES

As required by section 12A of the Federal Reserve Act, the time, character, and volume of all purchases and sales of obligations in the open market by Federal Reserve Banks are governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country.

### SECTION 270.4—TRANSACTIONS IN OBLIGATIONS

- (a) Each Federal Reserve Bank shall engage in open market operations under section 14 of the Federal Reserve Act only in accordance with this Part and with the authorizations and directives issued by the Committee from time to time, and no Reserve Bank shall decline to engage in open market operations as directed by the Committee.
- (b) Transactions for the System Open Market Account shall be executed by a Federal Reserve Bank selected by the Committee. The participations of the several Federal Reserve Banks in such Account and in the profits and losses on transactions for the Account shall be allocated in accordance with principles determined by the Committee from time to time.

- (c) In accordance with such limitations, terms, and conditions as are prescribed by law and in authorizations and directives issued by the Committee, the Reserve Bank selected by the Committee is authorized and directed—
- (1) To buy and sell Government securities and U. S. agency securities in the open market for the System Open Market Account, and to exchange maturing securities with the issuer;
- (2) To buy and sell bankers' acceptances in the open market for its own account;
- (3) To buy Government securities, U. S. agency securities, and bankers' acceptances of the kinds described above, under agreements for repurchase of such obligations, in the open market for its own account; and
- (4) To buy and sell foreign currencies in the form of cable transfers in the open market for the System Open Market Account and to maintain for such Account reciprocal currency arrangements with foreign banks among those designated by the Board of Governors of the Federal Reserve System under § 214.5 of this chapter [Regulation N].
- (d) In accordance with such limitations, terms, and conditions as are prescribed by law and in authorizations and directives insued by the Commitmittee, the Reserve Bank selected by the Commitmee (or, under special circumstances, such as when that Bank is closed, any other Federal Reserve Bank) is authorized and directed, for its own account or the System Open Market Account, to purchase directly from the United States such amounts of Government securities as may be necessary from time to time for the temporary accommodation of the Treasury Department.
- (d) (e) The Federal Reserve Banks are authorized and directed to engage in such other operations as the Committee may from time to time determine to be reasonably necessary to the effective conduct of open market operations and the effectuation of open market policies.