

(Superseded by 43)

FEDERAL RESERVE BANK
OF NEW YORK

NEW YORK, May 1, 1916.

TO THE CASHIER:

SIR:

Enclosed herewith is Circular No. 1, Series of 1916, addressed to member banks by the Federal Reserve Board, stating the principles upon which the Federal reserve banks shall establish a collection and clearing service for those of their member banks who desire to use it.

The preparation in detail of a collection and clearing plan embracing the entire country and including items on both national and state institutions will require careful study. A meeting of the transit managers of the twelve Federal reserve banks will be held in Chicago on May 8th for that purpose and you will be advised promptly of the details of the plan as soon as they have been approved.

Respectfully,

BENJ. STRONG, JR.,

Governor.

FEDERAL RESERVE BOARD.

WASHINGTON, *May 1, 1916.*

CHECK CLEARING AND COLLECTION.

To Member Banks:

The Federal Reserve Board is empowered, under section 16 of the Federal Reserve Act, to require each Federal Reserve Bank to—

“Exercise the function of a clearing house for its member banks.”

After very thorough investigation and many conferences with the Governors of the Federal Reserve Banks on this subject, the Federal Reserve Board has determined to exercise its authority and to offer to the member banks, and through them to the public, the machinery of the Federal Reserve Banks for the operation of a check collection and clearing system which it is believed, with the cooperation of member banks, will afford a direct, expeditious, and economical system of check collecting and settlement of balances.

The date for the inauguration of this system is expected to be June 15, 1916, or as soon thereafter as the Federal Reserve Banks can complete preparations for undertaking this work.

Member banks in each district will in due course receive from their Federal Reserve Bank full information as to the terms and all necessary details of the arrangement, but for the information of all concerned the general terms may be stated to be as follows:

(1) In order that no inconvenience may be experienced the plan will follow as closely as practicable the practice which long experience has developed between country banks and their reserve city correspondents.

Each Federal Reserve Bank will receive at par from its member banks checks drawn on all member banks, whether in its own district or other districts. It is also proposed to accept at par all checks drawn upon nonmember banks when such checks can be collected by the Federal Reserve Banks at par.

Each Federal Reserve Bank will receive at par from other Federal Reserve Banks checks drawn upon all member banks of its district and upon all nonmember banks whose checks can be collected at par by the Federal Reserve Bank.

It is the purpose of the Federal Reserve Board to have the collection system developed so as to embrace the collection of all checks on nonmember banks and private banks, and while this can not be done immediately, steps will be taken to afford these facilities as rapidly as possible. The Federal Reserve Banks will prepare a par list of all nonmember banks, to be revised from time to time, which will be furnished to member banks.

Immediate credit entry upon receipt subject to final payment will be made for all such items upon the books of the Federal Reserve Bank at full face value, but the proceeds will not be counted as reserve nor become available to meet checks drawn until actually collected, in accordance with the best practice now prevailing.

(2) Checks received by a Federal Reserve Bank on its member banks will be forwarded direct to such member banks and will not be charged to their accounts until advice of payment has been received or until sufficient time has elapsed within which to receive advice of payment.

(3) In the selection of collecting agents for handling checks on nonmember banks member banks will be given the preference.

(4) Under this plan Federal Reserve Banks will receive at par from their member banks checks on all member banks, and on nonmember banks whose checks can be collected at par by any Federal Reserve Bank. Member banks will be required by the Federal Reserve Board to provide funds to cover at par all checks received from, or for the account of, their Federal Reserve Banks: *Provided, however,* That a member bank may ship lawful money or Federal Reserve notes from its own vaults at the expense of its Federal Reserve Bank to cover any deficiency which may arise because of and only in the case of inability to provide items to offset checks received from or for the account of its Federal Reserve Bank.

(5) Section 19 of the Federal Reserve Act provides that—

“The reserve carried by a member bank with a Federal Reserve Bank may, under the regulations, and subject to such penalties as may be prescribed by the Federal Reserve Board, be checked against and withdrawn by such member bank for the purpose of meeting existing liabilities: *Provided, however,* That no bank shall at any time make new loans or shall pay any dividends unless and until the total reserve required by law is fully restored.”

It is manifest that items in process of collection can not lawfully be counted as reserve either by a member bank or by a Federal Reserve Bank. Therefore, should a member bank draw against such items the draft would be charged against its reserve if such reserve were sufficient in amount to pay it; but any resulting impairment of reserves would be subject to all the penalties provided by the Act.

Inasmuch as it is essential that the law in respect to the maintenance of required reserves by member banks shall be strictly complied with, the Federal Reserve Board will fix a penalty to be imposed upon member banks for encroaching upon their reserves.

Member banks can at all times arrange to keep their reserves intact by rediscounting with their Federal Reserve Bank.

(6). Each Federal Reserve Bank will determine by analysis the amounts of uncollected funds appearing on its books to the credit of each member bank. Such analysis will show the true status of the reserve held by the Federal Reserve Bank for each member bank and will enable it to apply the penalty for impairment of reserve.

A schedule of the time required within which to collect checks will be furnished to each member bank to enable it to determine the time at which any item sent to its Federal Reserve Bank will be counted as reserve and become available to meet any checks drawn.

(7) In handling items for member banks, a Federal Reserve Bank will act as agent only. It will require that each member bank authorize it to send checks for collection to banks on which checks are drawn, and, except for negligence, will assume no liability. Any further requirements that the Board may deem necessary will be set forth by the Federal Reserve Banks in their letters of instruction to their member banks.

(8) The cost of collecting and clearing checks must necessarily be borne by the banks receiving the benefit and in proportion to the service rendered. An accurate account will be kept by each reserve bank of the cost of performing this service and the Federal Reserve Board will, by rule, fix the charge, at so much per item, which may be imposed for the service of clearing or collection rendered by the reserve banks, as provided in section 16 of the Federal Reserve Act.

SHERMAN ALLEN,
Assistant Secretary.

CHARLES S. HAMLIN,
Governor.