

FEDERAL RESERVE BOARD

WASHINGTON

January 5, 1917

Mr. O. H. Wolfe,
Asst. Cashier, Philadelphia National Bank,
Philadelphia, Pa.

My dear Mr. Wolfe:

I read in a New York paper recently your very favorable comments on the subject of the check collection problem and, as I failed to keep the article, or mislaid it, I wish you would give me exact reference to it or send me a copy if you have one to spare. I should also like, at the same time, to have you make some suggestions as to how we can progress. In the opinion of some of our Federal Reserve Banks we are going ahead about as fast as we can and, in view of the agitation in Congress, it may not be wise for us to stir matters up until after the 4th of March. If, by that time, Mr. Jerome Thralls and the Committee of Twenty-five have not succeeded in their campaign, it should be up to us to make more successful progress. As Mr. Aiken, of the Boston Bank, writes, when he takes up with banks of his District the routing of more checks through his Bank, he is confronted by the statement that there are still so many non-par banks in the country whose checks cannot be handled through the Federal Reserve Bank that the maintenance of deposit accounts for collection purposes is still required, and he suggests that we ought to devise some way of securing the cooperation of the clearing houses in the various Districts, but I think I see some objection to this, even if it were possible, in the fact that the managers of the clearing houses, especially the country clearing houses, fear that the proposed method is going to supplant the old and that, on the theory of self-preservation, we find that they are naturally opposing in every way they can the progress of the system.

There are two of the twelve Districts in which the Federal Reserve Bank is collecting checks drawn on every member and nonmember bank. The Boston Bank was

able to take over a well established country clearing house, and the San Francisco Bank adopted the very bold project of agreeing to collect checks on any bank, and are using other banks and the express companies to effect this collection. While the actual volume of checks handled is not very large in the San Francisco District, the scheme has been wonderfully successful in breaking down non-par points.

Another system that has worked well in the Dallas District (and which is also to be tried in the Kansas City District) is where the reserve cities of the District are linked together in a scheme to interchange checks, the Federal Reserve Bank simply taking care of the net balances. The effect of this plan is to put the reserve cities of Texas, or the reserve cities of the Kansas City District, on a parity with the Federal Reserve City; that is, exchange on any one of the cities is interchangeable. Apparently, this scheme is only adaptable in a District where there are quite a number of reserve cities and where the banking is not highly centralized at the Federal Reserve center. Another way of dealing with the problem is to establish a scale of charges, not only between banks but between banks and their customers. This I consider a very drastic method and one which should not be used unless it was found necessary. I have prepared a draft of such a proposed schedule and enclose it herewith, not as expressing either the views of the Board, or my own final judgment, but simply as suggesting what might be done.

We recognize you as an expert on this question and would be very glad to have the benefit of your judgment.

Yours very truly,

F. A. Delano

Chairman, Committee on
Clearing

FEDERAL RESERVE BOARD
WASHINGTON

February 1, 1917

My dear Mr. Wolfe:

I have just discovered that I failed to acknowledge receipt of your letter of January 9th, in answer to mine in regard to the check collection matter. I want to thank you cordially for the trouble you have taken in going into this matter so fully. We realize, of course, the difficulties of the situation, but we are in hopes that we shall in the very near future be able to overcome the principal objections now in the way.

Yours very truly,

F. A. Delano

Mr. O. H. Wolfe
Philadelphia.

McLane Tilton, Jr.
Pell City, Ala.

Banking
Insurance
Law Office

January 8, 1917

Dear Mr. Wolfe:

I appreciate your letter of January 6, and no apologies were necessary about its length.

Most of the points you cover will be answered in a brief I have prepared which will be sent you shortly. Suffice now to refer to some others:

You say "Any bank that must depend for its existence on a continuation of past exchange conditions does not deserve to survive." Mr. Carter Glass holds the same theory, plus a general damnation for such institutions. I will take a chapter out of my personal experience as being typical.

I came here in 1902 when a box car and a tumble down building comprised its business structures. The county had about 18000 people, 90% white persons. It was the most illiterate county in the most illiterate state in the Union. There were no banks in the county, and the wealth was nihil. Homes, churches, schools and roads were even worse than you could expect from the description. This county is surrounded by four of the richest counties in Alabama, each of them containing one of the best towns in the state, Birmingham, Anniston, Talladega and Gadsden. Whatever service outside city banks could render St. Clair they had rendered or had the opportunity so to do for many years. Practically this was nihil also.

When I advised Mr. Harding, then president of the First of Birmingham, of my intention to start a bank at Pell City, he predicted ruin for the venture, declaring this county was a hopeless case from the business standpoint. After some months effort I placed 40 shares of stock with eight citizens in the county, taking what I could myself and borrowed on the balance in Chicago, no money obtainable in Birmingham.

This bank was a reasonable success from the start. Its officers in years intervening started four other banks in the county, in their home villages, resigning from our Board. In all ten banks were organized in the territory bounded by the four towns above named, where no banks existed in 1902.

What has been the result? The county has blossomed like a rose, property values and population have greatly increased, conditions of living have vastly improved, county and municipal government has become efficient, schools and roads are worthy of the name, the people are prosperous and happy, all of which can be attributed to the example, the influence and facilities of these banks. No other cause exists that was not effective before the banks came. Yet without income from exchange not one of these banks could have started, nor could they have survived if they did start, nor can they pay dividends today without this source of income.

What is true of this county is true of thousands of communities in the development of the United States in the past half century in the March of progress from the Blue Ridge to the Pacific.

Now the matter of the survival of these banks means more, much more than a loss to stockholders. It means the annihilation of credit to these communities,

the use of which has made them what they are and upon which their economic salvation still depends. This is true because no Bank in Birmingham or Anniston could or would render the facilities. To do so is utterly impossible, whether by branch banks or otherwise, and I say this from practical experience in the branch bank game. I went through that and was sufficiently burned to dread the fire.

So I again ask is not the trifling cost of exchange to city banks and business houses, which they can afford to pay and make profits undreamed of in the country, warranted if such results can be achieved?

The conditions which you describe as being intollerable some years back hardly square with the desperation with which city banks advertised and fought for collections. If the business was intollerable, or unprofitable, why accept it except on terms agreeable?

You say we want your public charged that our public may go free. This I deny. I do not want our public, however, saddled with the entire cost of the float as will inevitably happen if present tendencies are unchecked. And insomuch as there will always be some cost to the float, it should be carried by the strongest shoulders that can best bear it instead of shifted to the weakest.

You refer to time saved in collections. Possibly time is saved to city banks, another item of gain, but for country banks, three fourths of all of them, to route checks via the Federal means lost time as compared with the former routing.

If there have been a few hogs in the banking business, why not handle them directly, without drawing in the many institutions innocent of unfairness. It is most unusual to tax a witness with the costs of the law suit.

Who is to decide what is reasonable, you ask? Let the law decide it. I personally favor ten cents maximum per hundred. Mr. Kitchin approves this. I argued for it before the American Assn. Com. of 25 at Chicago Dec. 11 and the Kitchin bill, with my suggested amendment, was unanimously approved. No other man there save myself had a practical plan to offer.

Your argument as to how the Federal clears checks is ingenious but I think it can be definitely and conclusively shown that Federal Banks are charging collections against ledger reserve balances. Our own reserve has on several occasions been reported impaired when we have never drawn against it nor authorised our customers or the Federal so to do.

If you see no tangible reason, as you say, why state banks should not join the system, where are its many boasted advantages to members, or to the customers of members? Bankers, as quickly as any other class of men, avail themselves of improved economic facilities. That state banks have not joined proves how the pros and cons stand.

You mention the awful possibility of your return to country banking if "my" views prevail. Take a friendly tip and don't. However if such continues your determination I have two nationals on the market at about one half of what they were worth two years ago.

It is literally true that my banking business has been ruined, my main investment and source of living. I thought my boys would be on easy street, a good job for them and some dividends for myself when they were old enough to take hold which would be about time for me to quit. Am I to be blamed for pessimism, for

frothing at the mouth, for utilising the rights as a citizen to seek relief, to believe that I am just one of many entitled to it?

You say I would not swap places with a New York bank president. That was quite right up to the moment of the new dispensation. Now if you have a job handy that means modest comfort to a wife, two boys, an old black Mammy, a dry cow, chickens that won't lay, an Airdale, a crowd of bird dogs and fox hounds, plus friehgt on a house full of antique furniture, sing out by telegraph collect.

With all good wishes,

Yours sincerely,

McLane Tilton, Jr.

Mr. O. Howard Wolfe:

421 Chestnut Street
Philadelphia, January 9, 1917

Mr. F. A. Delano, Chairman Committee on Clearing,
Federal Reserve Board
Washington, D. C.

My dear Mr. Delano:-

I am sending you herewith the article you saw in the New York Times. I did not retain a copy and I am indebted to a friend for this clipping.

Your letter of the 5th does not admit of a ready reply, and I have delayed on answer hoping to be able to evolve at least one clear idea which might be of some assistance to you, but thus far, I am unable to suggest anything that seems to have any constructive merit. I am inclined to agree with those Reserve Banks which, as you state, are satisfied that you are going ahead as fast as conditions warrant. In any event, it is somewhat out of season to start any new developments till the Kitchin amendment is settled, one way or another. I presume the Reserve Board will see to it that Congress is well informed as to the merits of that bill.

In my opinion, you have gone about as far as you can so far as member banks are concerned, and you are now up against what has always appeared to me to be the vital weakness of the entire Reserve Act--the fact that it is law only for those who accept it as such. I do not mean that many minor changes and improvements in the present collection system may not suggest themselves, but I do mean that it will be a hard matter to make the collection system universal unless you first can induce or coerce non-members into it--or perhaps I should say educate them into it, assuming for argument's sake that it would be a good thing if all commercial banks at least were members.

At this point, so many issues arise and so many solutions may be proposed that the whole question is apt to scatter itself into a dozen abstract and academic discussions. If I may, I shall mention just a few as they occur to me.

First, are we agreed that the solution of the transit problem rests with the Reserve Banks? Personally I regret that the banks did not settle the matter independently, and then use the Reserve System somewhat as it is being used in the Dallas district--for the clearance of balances arising between natural collection centres. Coupled with this would be an adaptation of the Giro Conte system by which no bank need ever remit to another by draft, using book entries and Reserve Bank balances instead. It is going to be a very hard matter to break down the relationships that exist between city banks and correspondents and we of the big city banks are going to do everything we can to serve our country bank friends well. I doubt if the Reserve Banks can ever supplant us in this respect because we have the incentive of competition which they do not.

Another perplexing difficulty arises in trying to regulate the methods of member banks, where excesses have existed, so as not to injure them in competing with non-members not subject to control. I would certainly not advocate the plan to collect non-member checks at \$1.00 (or any other arbitrarily fixed rate) per thousand. This would only aggravate the present injustice, since you would pay a non-member this fee which he is at liberty to exact, and deny it to his neighbor across the street who must compete with him. At present, this same non-member can collect all his member checks at par, but can charge as he pleases for checks drawn on him and endorsed by these members. Have member banks been given an opportunity to remit

or cover for neighbor non-member checks? If not, that would seem to be a logical step to take, and instead of paying them a fee for this service you could afford to accept an offsetting amount of checks without charging them the regular service fee of $1\frac{1}{2}$ ¢ per item.

Has any consideration ever been given to putting a Federal tax on checks not collectible through the Reserve Banks? That may seem to be a bold proposition, but it is not so unreasonable as it sounds, and has a partial precedent in the old State bank note issues. As for the constitutionality of such a tax, let us consider what economic progress has been made since the Constitution prohibited states from coining or issuing money. Today we are issuing credit and credit instruments to cancel debt--the purpose of money--and the metal backing performs the function of reserve rather than that of a circulating medium as was the case a century ago. Mr. Warburg, I think, explained this dual function of money as "reserve" in his very excellent Kansas City address.

A more conservative policy which might produce good results would be to proceed, as at present, making minor improvements as they seem advisable and above all instilling the idea of service into the Reserve Banks, impressing upon them the wisdom of doing more rather than less, than can be expected of them by the banks which have created and own them. Experience and education by precept may be slow, but I believe if once the idea sinks in that the country bank should clear its checks with other country banks, just as the city banks clear with each other, the feeling against the Reserve collection system will disappear. Coupled with that, there should be a campaign against the payment of interest on uncollected balances, the payment of excessive rates of interest, and the use of uncollected funds. The New York Bank made an excellent start in this direction, but unfortunately undid much of the good by proposing a very complicated and unnecessarily cumbersome system of analysis.

If every means is taken to perfect what is now a very workable system, we may expect more and more pressure on state banks by their customers as they find their checks are discriminated against. This, too, is a slow process but we are beginning to see its effects already inside the banks. Terms now include special provisions for non-member items, and, if a few prominent clearing houses pass rules governing charges for such items, or if country clearing houses undertake to handle only such items as the Reserve Banks cannot collect, the problem may solve itself.

I thank you for the honor you do me in consulting me on this interesting problem and I regret that I can offer you nothing better at this time than a few random thoughts of no consequence.

Very truly yours,

O. Howard Wolfe

OHW.M.

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Author(s): O. Howard Wolfe

Title: Banking Legislation

Date: 1934

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Author(s): O. Howard Wolfe

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