

STATE BANKS IN FEDERAL RESERVE SYSTEM.

LETTER FROM THE GOVERNOR OF THE FEDERAL RESERVE BOARD TRANSMITTING, IN RESPONSE TO A SENATE RESOLUTION OF JANUARY 19, 1920, A COMMUNICATION SUBMITTING A REPORT AS TO ALLEGED COERCIVE MEASURES ATTEMPTED TO MAKE STATE BANKS SUBMIT TO RULES MADE BY THE FEDERAL RESERVE BOARD OR ANY FEDERAL RESERVE BANK.

JANUARY 28, 1920.—Referred to the Committee on Banking and Currency and ordered to be printed.

FEDERAL RESERVE BOARD,
Washington, January 26, 1920.

The PRESIDENT OF THE SENATE,
Washington, D. C.

SIR: I have the honor to acknowledge receipt of a resolution of the Senate of the United States, dated January 19, 1920—

Requesting the Federal Reserve Board to inform the Senate whether the board or any Federal reserve bank, under instructions or with the consent or knowledge of said board, has resorted to any method of coercion to compel State banks to join the Federal reserve system, or by threats or other coercive means has attempted to require such State banks to submit to any rules or regulations made by the Federal Reserve Board or any Federal reserve bank.

In order that the Senate may have a full and complete understanding of the position of the board with reference to the matters upon which it is understood information is requested in its resolution, the board desires to submit a brief review of the development of the system of check clearing and collection which is now in force in the several Federal reserve districts, together with a summary of those provisions of the law and the amendments thereto under which that system has been inaugurated and operated.

Section 16 of the Federal reserve act provides, in part, that the Federal Reserve Board—

May at its discretion exercise the functions of a clearing house for such Federal reserve banks * * * and may also require each such bank to exercise the functions of a clearing house for its member banks.

In accordance with what is understood to be the purpose of this provision of the law, the Federal Reserve Board, with the view ultimately of establishing a universal or national system of clearing intersectional balances as well as bank checks and drafts, has established a gold-settlement fund through which daily clearings between

all Federal reserve banks are consummated, and has also required each Federal reserve bank to exercise the functions of a clearing house for its member banks. The gold-settlement fund commenced operations in May, 1915, and has proved a remarkably effective medium for the expeditious and economical transfer of credits from one section of the country to another, thereby forming a delicate balance wheel tending to equalize interest rates in all sections. One year later in May, 1916, the Federal Reserve Board issued a circular, entitled "Check Clearing and Collection" (Exhibit A), to all member banks stating that under authority of section 16 of the Federal reserve act it would require each Federal reserve bank to "exercise the functions of a clearing house for its member banks," commencing June 15, 1916, or as soon thereafter as possible. The system was in fact inaugurated July 15, 1916. As outlined in that original circular the check collection facilities of each Federal reserve bank were at first to be limited primarily to "checks drawn on all member banks, whether in its own district or other districts," although it was stated that—

It is proposed to accept at par all checks drawn upon nonmember banks when such checks can be collected by the Federal reserve banks at par. * * * 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.

Immediately upon the inauguration of the system, the Federal Reserve Bank of Boston by reason of its having taken over the Boston Country Clearing House was able to collect checks drawn upon any bank, member or nonmember, located in New England, and in other districts many nonmember banks agreed to remit at par from the outset. (See press statement, July 18, 1916, issued by the board three days after the check collection system commenced its operations. Exhibit B.)

At that time—July, 1916—Federal reserve banks were expressly required by section 16 to "receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors." There was no option vested in the reserve banks. With reference to checks drawn upon nonmember banks the board had been advised by its counsel that although there was no provision of law expressly requiring a Federal reserve bank to receive for collection checks drawn upon such banks, they might properly do so, if they desired, in the exercise of their implied powers conferred by that part of section 4 which authorized them to exercise "such incidental powers as shall be necessary to carry on the business of banking within the limitations prescribed by this act." The right to receive checks for collection and credit is a right incidental both to the right to receive deposits and to the right to act as a "clearing house." In fact, all banking corporations, State and national, have almost universally exercised the right to collect checks as an incident to their general banking powers and without any express authority in the law. All the more justification is there for a Federal reserve bank to do so, because of its express power to act as a clearing house.

But even if there were ever any doubt as to that implied power, Congress on September 7, 1916, within three months after the inauguration of the original check collection system, amended section 13 by an act which, among other things, expressly permitted (but did not

require) Federal reserve banks to receive deposits of all "checks and drafts payable upon presentation." So that there can be no doubt as to the existing right of a reserve bank in its discretion to accept for collection checks drawn upon nonmember banks as well as checks upon member banks.

On June 21, 1917, Congress again amended the terms of section 13 by further defining the collection powers of Federal reserve banks. The purpose of that amendment was twofold. It was, first, to permit nonmember banks to become clearing members of the Federal reserve bank—that is, to permit such institutions to avail themselves of the privileges of the check collection system upon the maintenance with the reserve bank of a deposit sufficient to offset items in transit, without becoming regular members. That amendment was intended primarily for those nonmember banks which were ineligible for membership either because of a lack of sufficient capital or otherwise. It was, second, to permit both member and nonmember banks—

To make reasonable charges to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per \$100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise.

But it was expressly provided that—

No such charges shall be made against the Federal reserve banks.

This amendment is commonly referred to as the Hardwick amendment and represents the last change in the law in so far as it relates to the collection of checks.

Subsequent to its enactment the Federal Reserve Board issued the existing regulation on "Check clearing and collection (Exhibit C), the principal changes being those providing for the clearing of checks for those nonmember banks which desired to become clearing members under the act of June 21, 1917. Paragraph (1) of this regulation reads substantially as it did in the original circular:

Each Federal reserve bank will receive at par from its member banks and from nonmember banks in its district which have become clearing members, checks drawn on all member and clearing member banks and on all other nonmember banks which agree to remit at par through the Federal reserve bank of their district.

It will be noted that under the terms of this paragraph it is indicated that each Federal reserve bank will receive at par checks drawn on all member and clearing member banks and checks on all other nonmember banks which agree to remit at par.

Since that last amendment of Congress and the issue of the present regulations in accordance therewith the par collection list has grown gradually until at the present time checks on approximately 26,000 of the 30,000 banks of the country can be collected expeditiously and economically at par for the banks and through them for the public at large. In the development of this par list the Federal Reserve Board has made only such efforts as it deemed consistent with both the purposes of the law and the rights of the banks in general. It has never resorted to any method of coercion to compel State banks to join the Federal Reserve System nor has it by threats or other coercive means attempted to require such State banks to submit to rules or regulations made by the Federal Reserve Board or any Federal reserve bank. Furthermore, the board has never instructed or knowingly consented to any Federal reserve bank's adopting such means

in its efforts to extend its par list. Believing, however, that the purpose of the law itself and the needs and interests of the country as a whole would be better accommodated by the ability of the Federal reserve banks to collect for their member and clearing member banks all checks presented to them for that purpose, the board has consistently approved the efforts of the reserve banks to collect all checks upon whomsoever drawn, member banks, nonmember banks, or private banks, whether or not they agree in advance to remit at par.

But there are only three ways in which the holder of a check, whether an individual or a corporation, may lawfully and properly undertake its collections: (1) He may present it in person over the counter of the drawee bank for payment; (2) he may forward it to an agent more conveniently located geographically for the purpose of presentation through that agent to the drawee bank over its counter for payment; (3) he may forward it direct to the drawee bank for payment and remission therefor in cash or exchange.

The Federal reserve banks in the operation of their check-collection systems have followed the third course in the case of checks drawn on member and nonmember banks which may have agreed to remit at par either in cash or satisfactory exchange, and whether cash or exchange is remitted the Federal reserve banks have generally provided postage or necessary costs of transportation covering the shipment to the reserve bank. Because of the fact, however, that the so-called Hardwick amendment to section 13 not only prohibits a bank charging but also prohibits the Federal reserve bank paying a charge for the "payment or collection of checks and drafts and remission therefor by exchange or otherwise," Federal reserve banks have been impelled to forego the collection of checks in this manner in any case where the drawee bank does not care to remit at par. (See Opinions of the Attorney General of the United States, Exhibits D and E.) The only other available means of making the collection is to employ some suitable agent for that purpose. Not to adopt that means would necessitate a flat refusal by the reserve bank to handle the item for collection in any manner, and the board and the reserve banks feel that that would now be an evasion of one of the ultimate purposes for which the law was enacted; that is, the establishment of a universal country wide par-collection system and the resultant elimination of the burdensome delays and expenses incident to the old indirect routing system. In this connection the attention of the Senate is respectfully directed to a copy of a form letter which was sent by the Federal Reserve Board to nonmember banks and other parties interested defining the questions of law and policy involved in the matter of collecting all checks at par (Exhibit F).

When the par-collection system was first put into effect, it was impossible for practical reasons to undertake the collection of all checks drawn on nonmember banks, but now that there are relatively so few of those banks not on the par list the reserve banks are able usually to effect the collection of their checks by means of appropriate agents. There is no longer any reasonable excuse for refusing to handle such items for member and clearing-member banks wherever collection by means of an agent is practicable. This agent may be a member bank located in the same city as the drawee bank or possibly a nonmember bank, an express company, or any other suitable person

or corporation able to make the collection over the counter of the drawee bank.

The reserve banks in extending their collection facilities to include the checks of those nonmember banks which have declined to remit at par have generally, by letter or in person, undertaken to explain that the reserve banks could no longer decline to handle checks drawn upon those nonmember banks, and that inasmuch as they did not care to remit at par and inasmuch as the reserve bank could not lawfully pay exchange, it would be necessary to make their collections in the only other way legally possible over the counter either in cash or suitable exchange. But this explanation by the reserve bank has always been intended to be an expression of regret, not a threat—as some few banks have been only too glad to construe it. (Typical forms of letters used by the Federal reserve banks in this connection are attached hereto as Exhibit G.)

So far as the Federal Reserve Board is aware, the Federal reserve banks themselves have never been anything other than both patient and considerate in explaining the necessity for exercising what is after all an undisputed legal right to ask for payment over the counter—an inherent right in the holder of any check or bank draft. If in some few instances an agent of a reserve bank has, through an excess of zeal, adopted any other attitude in his efforts to procure par members or in explaining the unavoidable alternative that must be adopted by the reserve bank in the event that the nonmember bank does not want to remit at par, it has been without the authority or consent of either the Federal Reserve Board or the Federal reserve banks themselves.

It has been alleged that some of the reserve banks have intentionally held up items drawn on a nonmember bank for the purpose of presenting them in bulk and demanding payment in cash so as to embarrass the drawee bank and thus compel it to remit at par. In order fully to advise the Senate on this particular matter the Board, upon receipt of the Senate's resolution, telegraphed to each Federal reserve bank (Exhibit H) specifically requesting to be advised whether or not such methods had been employed, and if so with what purpose. The replies of the several reserve banks are attached hereto (Exhibit I).

In this connection the attention of the Senate is respectfully directed particularly to the reply of the Federal Reserve Bank of Kansas City. This telegram, it is believed, indicates the obstacles which were arbitrarily placed in the way of the Federal reserve bank in the making of its collections in the more usual manner and explains to some extent the reason that the Federal reserve bank in that instance was impelled to send its own agents at stated intervals to make the necessary collection of items which had been forwarded to it by its member banks. While that telegram from the Federal Reserve Bank of Kansas City, as well as the replies from the Federal reserve banks of Dallas, Minneapolis, and Chicago indicate that in a few instances they have accumulated checks when collecting through an agent, it has never been for the purpose of embarrassing the drawee bank, but has been done solely in pursuance of a practice generally followed by large commercial banks in various parts of the country either on account of the physical difficulty of sending a daily messenger or because of the relatively high overhead charge in sending a messenger to collect a small check. But even instances

of that nature were reported by only 4 of the 12 Federal reserve banks and are not general practices in the case of those 4. The replies of the banks themselves are explanatory of their purpose.

In conclusion the Federal Reserve Board desires to state that the development of the Federal reserve par collection system has been the result of the most conscientious and painstaking thought and efforts of the board and officers of the several Federal reserve banks with the sole purpose not of compelling a relatively few unwilling State banks to become clearing members but of affording to the great majority of banks in the country the member and clearing member banks, now over 26,000 out of approximately 30,000, a complete and effective system of check collection involving a minimum of effort, time, and expense, a system whose facilities are now offered free of charge to the banks of the country and through them to the public at large. The burden that some banks have in the past put upon the commerce of the country through arbitrary and excessive exchange charges does not need comment.

That a relatively small number of nonmember banks should not want to become members of the clearing system or should not want to remit at par is, of course, their own concern and the Federal Reserve Board and the Federal reserve banks have not and will not dispute their right to decline to do so. But that those same few nonmember banks, which through their member bank correspondents are able to obtain the benefits of the par collection system gratis, should decline to become clearing members can not and should not deter the Federal reserve banks in the exercise of their undoubted legal right—the right to collect over the counter in cash or satisfactory exchange, by means of an agent, checks drawn upon a bank which for one reason or another does not care to remit at par for checks mailed to it directly.

The Federal Reserve Board submits this report of the steps taken by it to put into effect these provisions of the Federal reserve act which they believe will in time prove to be one of its greatest benefits—a universal country-wide system of par check collections scientifically conceived by Congress and expeditiously and economically operated by the Federal reserve banks in the interest of the country at large without discrimination in favor of any one class or classes.

Respectfully submitted.

W. P. G. HARDING, *Governor.*

EXHIBIT A.

CIRCULAR No. 1.
SERIES OF 1916

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 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 arrangements 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 his 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.

CHARLES S. HAMLIN,
Governor.
SHERMAN ALLEN,
Assistant Secretary.

EXHIBIT B.

PRESS STATEMENT.

JULY 18, 1916.

The Federal Reserve Board gave out the following statement to-day:

"The new country-wide clearing system was inaugurated on July 15 in all the Federal reserve banks. Reports as of the close of business on July 17 show that the operations started out in a very satisfactory manner, and it is especially gratifying to the board to record the cordial cooperation of banks and bankers. The public doubtless understands that through this method all national banks and all State banks which are members of the Federal Reserve System have the privilege of using the Federal reserve banks as clearing houses for the clearing and collection of checks. Not only may checks drawn against other member banks be collected at par, but checks drawn against most nonmember banks can also be so collected at a minimum of expense to the depositing bank.

"The Boston district, by reason of having taken over the Boston Country Clearing House, was able to make the most flattering exhibit, so that in New England checks drawn against a bank, whether member or nonmember, are collected at par without exception. In the other districts there is no difficulty in collecting checks at par, even when drawn against nonmember State banks, provided there are national banks in the same city or town. There is more difficulty where these State banks are located in towns where there are no national or other member banks, but even in these cases, the reports in the hands of the board show that a very large percentage of nonmember State banks have agreed to remit at full face value through the Federal reserve banks.

"Some time must necessarily elapse before the new collection system will be used to its capacity, but the Federal Reserve Board believes confidently that the country has now witnessed the inauguration of the most effective check collection system that has ever been devised, and that each passing week will add to the use and appreciation of the system by the banking and business communities of the country."

EXHIBIT C.

[Federal Reserve Board. Regulations Series of 1917. June, 1917.]

FEDERAL RESERVE BOARD,
Washington, June 22, 1917.

The Federal Reserve Board transmits herewith a new issue of all of its regulations of 1916 applicable to member banks. This revision was necessitated by the enactment of the recent amendments to the Federal reserve act.

Regulations C, H, and J have been materially altered because of those amendments. Regulation D has been amended so as to include postal savings deposits in the definition of a "time deposit" as required by the recent amendment to section 19. Regulation G has been amended by adding a paragraph relating to the renewal of loans upon the security of real estate. Regulations A, B, E, F, and I are identically the same as last year.

Instructions which concern only Federal reserve agents or Federal reserve banks will be covered in separate letters or regulations, as in the past.

W. P. G. HARDING, *Governor.*
H. PARKER WILLIS, *Secretary.*

STATE BANKS IN FEDERAL RESERVE SYSTEM.

REGULATION A.
SERIES OF 1917.
(Superseding Regulation A of 1916.)

REDISCOUNTS UNDER SECTION 13.

A.

NOTES, DRAFTS, AND BILLS OF EXCHANGE.

I. *General statutory provisions.*

Any Federal Reserve Bank may discount for any of its member banks any note, draft, or bill of exchange provided—

(a) It has a maturity at the time of discount of not more than 90 days, exclusive of days of grace; but if drawn or issued for agricultural purposes or based on live stock, it may have a maturity at the time of discount of not more than six months, exclusive of days of grace.

(b) It arose out of actual commercial transactions; that is, it must be a note, draft, or bill of exchange which has been issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used or are to be used for such purposes.

(c) It was not issued for carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States.

(d) The aggregate of notes, drafts, and bills bearing the signature or indorsement of any one borrower, whether a person, company, firm, or corporation rediscounted for any one member bank shall at no time exceed 10 per cent of the unimpaired capital and surplus of such bank; but this restriction shall not apply to the discount of bills of exchange drawn in good faith against actually existing values.

(e) It is indorsed by a member bank.

(f) It conforms to all applicable provisions of this regulation.

II. *General character of notes, drafts, and bills of exchange eligible.*

The Federal Reserve Board, exercising its statutory right to define the character of a note, draft, or bill of exchange eligible for rediscount at a Federal reserve bank, has determined that—

(a) It must be a note, draft, or bill of exchange the proceeds of which have been used or are to be used in producing, purchasing, carrying, or marketing goods¹ in one or more of the steps of the process of production, manufacture, or distribution.

(b) It must not be a note, draft, or bill of exchange the proceeds of which have been used or are to be used for permanent or fixed investments of any kind, such as land, buildings, or machinery.

(c) It must not be a note, draft, or bill of exchange the proceeds of which have been used or are to be used for investments of a purely speculative character.

(d) It may be secured by the pledge of goods or collateral, provided it is otherwise eligible.

III. *Applications for rediscount.*

All applications for the rediscount of notes, drafts, or bills of exchange must contain a certificate of the member bank, in form to be prescribed by the Federal reserve bank, that, to the best of its knowledge and belief, such notes, drafts, or bills of exchange have been issued for one or more of the purposes mentioned in II (a).

IV. *Promissory notes.*

(a) *Definition.*—A promissory note, within the meaning of this regulation, is defined as an unconditional promise, in writing, signed by the maker, to pay, in the United States, at a fixed or determinable future time, a sum certain in dollars to order or to bearer.

(b) *Evidence of eligibility and requirement of statements.*—A Federal reserve bank must be satisfied by reference to the note or otherwise that it is eligible for rediscount. Compliance of a note with II (b) may be evidenced by a statement of the borrower

¹ When used in this regulation the word "goods" shall be construed to include goods, wares, merchandise or agricultural products, including live stock.

showing a reasonable excess of quick assets over current liabilities. The member bank shall certify in its application whether the note offered for rediscount has been discounted for a depositor or another member bank or whether it has been purchased from a nondepositor. It must also certify whether a financial statement of the borrower is on file.

Such financial statements must be on file with respect to all notes offered for rediscount which have been purchased from sources other than a depositor or a member bank. With respect to any other note offered for rediscount, if no statement is on file, a Federal reserve bank shall use its discretion in taking the steps necessary to satisfy itself as to eligibility. It is authorized to waive the requirement of a statement with respect to any note discounted by a member bank for a depositor or another member bank—

(1) If it is secured by a warehouse, terminal, or other similar receipt covering goods in storage;

(2) If the aggregate of obligations of the borrower rediscounted and offered for rediscount at the Federal reserve bank is less than a sum equal to 10 per cent of the paid-in capital of the member bank and does not exceed \$5,000.

V. Drafts, bills of exchange, and trade acceptances.

(a) *Definition.*—A draft or bill of exchange, within the meaning of this regulation is defined as an unconditional order in writing, addressed by one person to another, other than a banker as defined under B (b), signed by the person giving it, requiring the person to whom it is addressed, to pay, in the United States, at a fixed or determinable future time, a sum certain in dollars to the order of a specified person; and a trade acceptance is defined as a draft or bill of exchange drawn by the seller on the purchaser of goods sold and accepted by such purchaser.

(b) *Evidence of eligibility.*—A Federal reserve bank shall take such steps as it deems necessary to satisfy itself as to the eligibility of the draft or bill offered for rediscount, unless it presents prima facie evidence thereof or bears a stamp or certificate affixed by the acceptor or drawer showing that it is a trade acceptance.

VI. Six months' agricultural paper.

(a) *Definition.*—Six months' agricultural paper, within the meaning of this regulation, is defined as a note, draft, bill of exchange, or trade acceptance drawn or issued for agricultural purposes, or based on live stock; that is, a note, draft, bill of exchange, or trade acceptance the proceeds of which have been used, or are to be used, for agricultural purposes, including the breeding, raising, fattening, or marketing of live stock, and which has a maturity at the time of discount of not more than six months, exclusive of days of grace.

(b) *Eligibility.*—To be eligible for rediscount six months' agricultural paper, whether a note, draft, bill of exchange, or trade acceptance, must comply with the respective sections of this regulation which would apply to it if its maturity were 90 days or less

VII. Commodity paper.

(a) *Definition.*—Commodity paper within the meaning of this regulation is defined as a note, draft, bill of exchange, or trade acceptance accompanied and secured by shipping documents or by a warehouse, terminal, or other similar receipt covering approved and readily marketable, nonperishable staples properly insured.

(b) *Eligibility.*—To be eligible for rediscount at the special rates, authorized to be established for commodity paper, such a note, draft, bill of exchange, or trade acceptance must also comply with the respective sections of this regulation applicable to it, must conform to the requirements of the Federal reserve bank relating to shipping documents, receipts, insurance, etc., and must be a note, draft, bill of exchange, or trade acceptance on which the rate of interest or discount, including commission, charged the maker does not exceed 6 per cent per annum.

(c) *Suspension of commodity rate.*—As the special rate on commodity paper is intended to assist actual producers during crop-moving periods and is not designed to benefit speculators, the board reserves the right to suspend the special rates herein provided whenever it is apparent that the movement of crops, which this rate is intended to facilitate, has been practically completed.

B.

BANKERS' ACCEPTANCES.

(a) *General statutory provisions.*—Any Federal reserve bank may discount for any of its member banks bankers' acceptances which have a maturity at the time of discount of not more than three months' sight, exclusive of days of grace, which are indorsed by at least one member bank, and which grow out of transactions involving the importation or exportation of goods, or which grow out of transactions involving the domestic shipment of goods, provided shipping documents are attached at the time of acceptance, or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. Any Federal reserve bank may also acquire drafts or bills of exchange drawn on member banks by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange.

(b) *Definition.*—A banker's acceptance within the meaning of this regulation is defined as a draft or bill of exchange of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged in the business of granting bankers' acceptance credits.

(c) *Eligibility.*—To be eligible for rediscount the bill must have been drawn under a credit opened for the purpose of conducting or settling accounts resulting from a transaction or transactions involving (1) the shipment of goods between the United States and any foreign country, or between the United States and any of its dependencies or insular possessions, or between foreign countries, or (2) the domestic shipment of goods, provided shipping documents are attached at the time of acceptance; or it must be a bill which is secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. Any Federal reserve bank may also acquire drafts or bills drawn by a bank or banker in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange and accepted by a member bank in accordance with the provisions of Regulation C, following. Such drafts or bills may be acquired prior to acceptance, provided they have the indorsement of a member bank.

(d) *Evidence of eligibility.*—A Federal reserve bank must be satisfied, either by reference to the acceptance itself or otherwise, that it is eligible for rediscount. Satisfactory evidence of eligibility may consist of a stamp or certificate affixed by the acceptor in form satisfactory to the Federal reserve bank.

REGULATION B.
SERIES OF 1917.
(Superseding Regulation B of 1916.)

OPEN-MARKET PURCHASES OF BILLS OF EXCHANGE, TRADE ACCEPTANCES, AND
BANKERS' ACCEPTANCES UNDER SECTION 14.

I. *General statutory provisions.*

Section 14 of the Federal reserve act permits Federal reserve banks, under rules and regulations to be prescribed by the Federal Reserve Board, to purchase and sell in the open market from banks, firms, corporations, or individuals bankers' acceptances and bills of exchange of the kinds and maturities made eligible by the act for rediscount, with or without the indorsement of a member bank.

II. *General character of bills and acceptances eligible.*

The Federal Reserve Board, exercising its statutory right to regulate the purchase of bills of exchange and acceptances, has determined that a bill of exchange or acceptance, to be eligible for purchase by Federal reserve banks under section 14—

(a) Must not have been issued for carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States.

(b) Must not be a bill the proceeds of which have been used or are to be used for permanent or fixed investments of any kind, such as land, buildings, or machinery, or for investments of a merely speculative character.

(c) Must have been accepted by the drawee prior to purchase by a Federal reserve bank unless it is accompanied and secured by shipping documents or by a warehouse, terminal, or other similar receipt conveying security title.

(d) May be secured by the pledge of goods¹ or collateral, provided it is otherwise eligible.

¹ When used in this regulation the word "goods" shall be construed to include goods, wares, merchandise, or agricultural products, including live stock.

In addition to the above general requirements, each bill of exchange and trade acceptance purchased under the terms of this regulation must also conform to the more specific requirements set forth under III, and each banker's acceptance must also conform to the more specific requirements set forth under IV.

III. Bills of exchange and trade acceptances.

(a) *Definition.*—A bill of exchange, within the meaning of this regulation, is defined as an unconditional order in writing, addressed by one person to another, other than a banker as defined under IV (a), signed by the person giving it, requiring the person to whom it is addressed to pay, in the United States, at a fixed or determinable future time, a sum certain in dollars to the order of a specified person; and trade acceptance is defined as a bill of exchange drawn by the seller on the purchaser of goods sold, and accepted by such purchaser.

(b) *Eligibility.*—To be eligible for purchase the bill must have arisen out of an actual commercial transaction, domestic or foreign; that is, it must be a bill which has been issued or drawn for agricultural, industrial, or commercial purposes or the proceeds of which have been used or are to be used for the purpose of producing, purchasing, carrying, or marketing goods in one or more of the steps of the process of production, manufacture, or distribution. It must have a maturity at time of purchase of not more than 90 days, exclusive of days of grace.

(c) *Evidence of eligibility.*—A Federal reserve bank shall take such steps as it deems necessary to satisfy itself as to the eligibility of the bill offered for purchase, unless it presents prima facie evidence thereof or bears a stamp or certificate affixed by the acceptor or drawer showing that it is a trade acceptance.

(d) *Statements.*—Unless indorsed by a member bank, a bill is not eligible for purchase until a satisfactory statement has been furnished of the financial condition of one or more of the parties thereto.

IV. Bankers' acceptances.

(a) *Definition.*—A banker's acceptance, within the meaning of this regulation, is a bill of exchange of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged in the business of granting bankers' acceptance credits.

(b) *Eligibility.*—To be eligible for purchase, the bill which must have a maturity at time of purchase of not more than three months, exclusive of days of grace, must have been drawn under a credit opened for the purpose of conducting, or settling accounts resulting from, a transaction or transactions involving—

- (1) The shipment of goods between the United States and any foreign country, or between the United States and any of its dependencies or insular possessions, between foreign countries, or
- (2) The shipment of goods within the United States, provided the bill at the time of its acceptance is accompanied by shipping documents, or
- (3) The storage within the United States of readily marketable goods, provided the acceptor of the bill is secured by warehouse, terminal, or other similar receipt, or
- (4) The storage within the United States of goods which have been actually sold, provided the acceptor of the bill is secured by the pledge of such goods; or it must be a bill drawn by a bank or banker in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange. In this latter case the bank or banker drawing the bill must be in a country, dependency, or possession whose usages of trade have been determined by the Federal Reserve Board to require the drawing of bills of this character.

(c) *Evidence of eligibility.*—A Federal reserve bank must be satisfied either by reference to the acceptance itself, or otherwise, that it is eligible for purchase. Satisfactory evidence of eligibility may consist of a stamp or certificate affixed by the acceptor, in form satisfactory to the Federal reserve bank. No evidence of eligibility is required with respect to a bill accepted by a national bank.

(d) *Statements.*—Bankers' acceptances, other than those accepted or indorsed by member banks, shall be eligible for purchase only after the acceptor has furnished a satisfactory statement of financial condition in form to be approved by the Federal Reserve Board and has agreed in writing with a Federal reserve bank to inform it upon request concerning the transactions underlying such acceptances.

REGULATION C.
SERIES OF 1917.
(Superseding Regulation C of 1916.)

ACCEPTANCE BY MEMBER BANKS OF DRAFTS AND BILLS OF EXCHANGE.

A.

ACCEPTANCE OF DRAFTS OR BILLS OF EXCHANGE DRAWN AGAINST DOMESTIC OR FOREIGN SHIPMENTS OF GOODS OR SECURED BY WAREHOUSE RECEIPTS COVERING READILY MARKETABLE STAPLES.

I. *Statutory provisions.*

Under the provisions of the fifth paragraph of section 13 of the Federal reserve act, as amended by the acts of September 7, 1916, and June 21, 1917, any member bank may accept drafts or bills of exchange drawn upon it, having not more than six months' sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods, provided shipping documents conveying or securing title are attached at the time of acceptance: or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. This paragraph limits the amount which any bank shall accept for any one person, company, firm, or corporation, whether in a foreign or domestic transaction, to an amount not exceeding at any time, in the aggregate, more than 10 per cent of its paid-up and unimpaired capital stock and surplus. This limit, however, does not apply in any case where the accepting bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance. The law also provides that any bank may accept such bills up to an amount not exceeding at any time, in the aggregate, more than one-half of its paid-up and unimpaired capital stock and surplus; or, with the approval of the Federal Reserve Board, up to an amount not exceeding at any time, in the aggregate, more than 100 per cent of its paid-up and unimpaired capital stock and surplus. In no event, however, shall the aggregate amount of acceptances growing out of domestic transactions exceed 50 per cent of such capital stock and surplus.

II. *Regulations.*

1. Under the provisions of the law referred to above the Federal Reserve Board has determined that any member bank, having an unimpaired surplus equal to at least 20 per cent of its paid-up capital, which desires to accept drafts or bills of exchange drawn for the purposes described above, up to an amount not exceeding at any time, in the aggregate, 100 per cent of its paid-up and unimpaired capital stock and surplus, may file an application for that purpose with the Federal Reserve Board. Such application must be forwarded through the Federal reserve bank of the district in which the applying bank is located.

2. The Federal reserve bank shall report to the Federal Reserve Board upon the standing of the applying bank, stating whether the business and banking conditions prevailing in its district warrant the granting of such applications.

3. The approval of any such application may be rescinded upon 90 days' notice to the bank affected.

B.

ACCEPTANCE OF DRAFTS OR BILLS OF EXCHANGE DRAWN FOR THE PURPOSE OF CREATING DOLLAR EXCHANGE.

I. *Statutory provisions.*

Section 13 of the Federal reserve act also provides that any member bank may accept drafts or bills of exchange drawn upon it having not more than three months' sight to run, exclusive of days of grace, drawn, under regulations to be prescribed by the Federal Reserve Board, by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries, dependencies, or insular possessions.

No member bank shall accept such drafts or bills of exchange for any one bank to an amount exceeding in the aggregate 10 per cent of the paid-up and unimpaired cap-

ital and surplus of the accepting bank unless the draft or bill of exchange is accompanied by documents conveying or securing title or by some other adequate security. No member bank shall accept such drafts or bills in an amount exceeding at any time in the aggregate one-half of its paid-up and unimpaired capital and surplus. This 50 per cent limit is separate and distinct from and not included in the limits placed upon the acceptance of drafts and bills of exchange as described under section A of this regulation.

II. Regulations.

Any member bank desiring to accept drafts drawn by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange shall first make an application to the Federal Reserve Board setting forth the usages of trade in the respective countries, dependencies, or insular possessions in which such banks or bankers are located.

If the Federal Reserve Board should determine that the usages of trade in such countries, dependencies, or possessions require the granting of the acceptance facilities applied for, it will notify the applying bank of its approval and will also publish in the Federal Reserve Bulletin the name or names of those countries, dependencies, or possessions in which banks or bankers are authorized to draw on member banks whose applications have been approved for the purpose of furnishing dollar exchange.

The Federal Reserve Board reserves the right to modify, or, on 90 days' notice to revoke, its approval either as to any particular member bank or as to any foreign country or dependency or insular possession of the United States in which it has authorized banks or bankers to draw on member banks for the purpose of furnishing dollar exchange.

REGULATION D.
SERIES OF 1917.
(Superseding Regulation D of 1916.)

TIME DEPOSITS AND SAVINGS ACCOUNTS.

Section 19 of the federal reserve act provides, in part, as follows:

Demand deposits, within the meaning of this act, shall comprise all deposits payable within 30 days, and time deposits shall comprise all deposits payable after 30 days, and all savings accounts and certificates of deposit which are subject to not less than 30 days' notice before payment, and all postal-savings deposits.

TIME DEPOSITS, OPEN ACCOUNTS.

The term "time deposits, open accounts" shall be held to include all accounts, not evidenced by certificates of deposit or savings pass books, in respect to which a written contract is entered into with the depositor at the time the deposit is made that neither the whole nor any part of such deposit may be withdrawn by check or otherwise, except on a given date or on written notice given by the depositor a certain specified number of days in advance, in no case less than 30 days.

SAVINGS ACCOUNTS.

The term "savings accounts" shall be held to include those accounts of the bank in respect to which, by its printed regulations, accepted by the depositor at the time the account is opened—

- (a) The pass book, certificate, or other similar form of receipt must be presented to the bank whenever a deposit or withdrawal is made, and
- (b) The depositor may at any time be required by the bank to give notice of an intended withdrawal not less than 30 days before a withdrawal is made.

TIME CERTIFICATES OF DEPOSIT.

A "time certificate of deposit" is defined as an instrument evidencing the deposit with a bank, either with or without interest, of a certain sum specified on the face of the certificate payable in whole or in part to the depositor or on his order—

- (a) On a certain date, specified on the certificate, not less than 30 days after the date of the deposit, or
- (b) After the lapse of a certain specified time subsequent to the date of the certificate, in no case less than 30 days, or
- (c) Upon written notice given a certain specified number of days, not less than 30 days before the date of repayment, and
- (d) In all cases only upon presentation of the certificate at each withdrawal for proper indorsement or surrender.

REGULATION E.
SERIES OF 1917.
(Superseding Regulation E of 1916.)

PURCHASE OF WARRANTS.

STATUTORY REQUIREMENTS.

Section 14 of the Federal reserve act reads in part as follows:

Every Federal reserve bank shall have power—

(b) To buy and sell, at home or abroad, bonds and notes of the United States, and bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months, issued in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by any State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage, and reclamation districts, such purchases to be made in accordance with rules and regulations prescribed by the Federal Reserve Board.

For brevity's sake, the term "warrant" when used in this regulation shall be construed to mean "bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months," and the term "municipality" shall be construed to mean "State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage, and reclamation districts."

REGULATION.

I. Any Federal reserve bank may purchase warrants issued by a municipality in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues, provided—

- (a) They are the general obligations of the entire municipality; it being intended to exclude as ineligible for purchase all such obligations as are payable from "local benefit" and "special assessment" taxes when the municipality at large is not directly or ultimately liable;
- (b) They are issued in anticipation of taxes or revenues which are due and payable on or before the date of maturity of such warrants; but the Federal Reserve Board may waive this condition in specific cases. For the purposes of this regulation, taxes shall be considered as due and payable on the last day on which they may be paid without penalty;
- (c) They are issued by a municipality—
 - (1) Which has been in existence for a period of 10 years;
 - (2) Which for a period of 10 years previous to the purchase has not defaulted for longer than 15 days in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it;
 - (3) Whose net funded indebtedness does not exceed 10 per cent of the valuation of its taxable property, to be ascertained by the last preceding valuation of property for the assessment of taxes.

II. Except with the approval of the Federal Reserve Board, no Federal reserve bank shall purchase and hold an amount in excess of 25 per cent of the total amount of warrants outstanding at any time and issued in conformity with provisions of section 14 (b) above quoted, and actually sold by a municipality.

III. Except with the approval of the Federal Reserve Board, the aggregate amount invested by any Federal reserve bank in warrants of all kinds shall not exceed at the time of purchase a sum equal to 10 per cent of the deposits kept by its member banks with such Federal reserve bank.

IV. Except with the approval of the Federal Reserve Board, the maximum amount which may be invested at the time of purchase by any Federal reserve bank in warrants of any single municipality shall be limited to the following percentages of the deposits kept in such Federal reserve bank by its member banks:

- Five per cent of such deposits in warrants of a municipality of 50,000 population or over;
- Three per cent of such deposits in warrants of a municipality of over 30,000 population but less than 50,000;
- One per cent of such deposits in warrants of a municipality of over 10,000 population but less than 30,000.

V. Warrants of a municipality of 10,000 population or less shall be purchased only with the special approval of the board.

The population of a municipality shall be determined by the last Federal or State census. Where it can not be exactly determined, the board will make special rulings.

VI. Opinion of recognized counsel on municipal issues or of the regularly appointed counsel of the municipality as to the legality of the issue shall be secured and approved in each case by counsel for the Federal reserve bank.

VII. Any Federal reserve bank may purchase from any of its member banks warrants of any municipality, indorsed by such member bank, with waiver of demand, notice, and protest, up to an amount not to exceed 10 per cent of the aggregate capital and surplus of such member bank: *Provided, however*, That such warrants comply with provisions I and III of these regulations, except that where a period of 10 years is mentioned in I (c) hereof a period of 5 years shall be substituted for the purposes of this clause.

REGULATION F.
SERIES OF 1917.
(Superseding Regulation F of 1916.)

TRUST POWERS OF NATIONAL BANKS.

I. *Statutory provisions.*

The Federal reserve act provides:

SEC. 11. The Federal Reserve Board shall be authorized and empowered:

(k) To grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, or registrar of stocks and bonds, under such rules and regulations as the said board may prescribe.

II. *Applications.*

A national bank desiring to exercise any or all of the privileges authorized by section 11, subsection (k), of the Federal reserve act shall make application to the Federal Reserve Board on a form approved by said board (Form No. 61). Such application shall be forwarded by the applying bank to the chairman of the board of directors of the Federal reserve bank of its district, and shall thereupon be transmitted to the Federal Reserve Board with his recommendations.

III. *Separate departments.*

Every national bank permitted to act under this section shall establish a separate trust department, and shall place such department, under the management of an officer or officers, whose duties shall be prescribed by the board of directors of the bank.

IV. *Provision for keeping trust funds.*

The funds, securities, and investments held in each trust shall be held separate and distinct from the general funds and securities of the bank, and separate and distinct one from another. The ledgers and other books kept for the trust department shall be entirely separate and apart from the other books and records of the bank.

V. *Examinations.*

Examiners appointed by the Comptroller of the Currency or designated by the Federal Reserve Board will hereafter be instructed to make thorough and complete audits of the cash, securities, accounts, and investments of the trust department of every bank at the same time that examination is made of the banking department.

VI. *Conformity with State laws.*

Nothing in these regulations shall be construed to give to a national bank doing business as trustee, executor, administrator, or registrar of stocks and bonds under section 11 (k) of the Federal reserve act any rights or privileges in contravention of the laws of the State in which the bank is located.

VII. *Revocation of permits.*

The Federal Reserve Board reserves the right to revoke permits granted under these regulations in any case where in the opinion of the board a bank has willfully violated the provisions of these regulations or the laws of any State relating to the operations of such bank when acting as trustee, executor, administrator, or registrar of stocks and bonds.

VIII. *Changes in rules.*

These regulations are subject to change by the Federal Reserve Board: *Provided, however*, That no such change shall prejudice obligations undertaken in good faith under regulations in effect at the time the obligation was assumed.

REGULATION G.
SERIES OF 1917.
(Superseding Regulation G of 1916.)

LOANS ON FARM LAND AND OTHER REAL ESTATE.

Section 24 of the Federal reserve act provides in part that—

“Any national banking association not situated in a central reserve city may make loans secured by improved and unencumbered farm land situated within its Federal reserve district or within a radius of 100 miles of the place in which such bank is located, irrespective of district lines, and may also make loans secured by improved and unencumbered real estate located within 100 miles of the place in which such bank is located, irrespective of district lines; but no loan made upon the security of such farm land shall be made for a longer time than five years, and no loan made upon the security of such real estate as distinguished from farm land shall be made for a longer time than one year nor shall the amount of any such loan, whether upon such farm land or upon such real estate, exceed 50 per cent of the actual value of the property offered as security. Any such bank may make such loans, whether secured by such farm land or such real estate, in an aggregate sum equal to 25 per cent of its capital and surplus or to one-third of its time deposits, and such banks may continue hereafter as heretofore to receive time deposits and to pay interest on the same.”

National banks not located in central reserve cities may, therefore, legally make loans secured by improved and unencumbered farm land or other real estate as provided by this section.

Certain conditions and restrictions must, however, be observed—

(a) There must be no prior lien on the land; that is, the lending bank must hold an absolute first mortgage or deed of trust.

(b) The amount of the loan must not exceed 50 per cent of the actual value of the land by which it is secured.

(c) The maximum amount of loans which a national bank may make on real estate, whether on farm land or on other real estate as distinguished from farm land, is limited under the terms of the act to an amount not in excess of one-third of its time deposits at the time of the making of the loan, and not in excess of one-third of its average time deposits during the preceding calendar year: *Provided, however*, That if one-third of such time deposits as of the date of making the loan or one-third of the average time deposits for the preceding calendar year, is less than one-fourth of the capital and surplus of the bank as of the date of making the loan, the bank in such event shall have authority to make loans upon real estate under the terms of the act to the extent of one-fourth of the bank's capital and surplus as of that date.

(d) Farm land to be eligible as security for a loan by a national bank must be situated within the Federal reserve district in which such bank is located or within a radius of 100 miles of such bank, irrespective of district lines.

(e) Real estate as distinguished from farm land to be eligible as security for a loan by a national bank must be located within a radius of 100 miles of such bank, irrespective of district lines.

(f) The right of a national bank to “make loans” under section 24 includes the right to purchase or discount loans already made as well as the right to make such loans in the first instance: *Provided, however*, That no loan secured by farm land shall have a maturity of more than five years from the date on which it was purchased or made by the national bank and that no loan secured by other real estate shall have a maturity of more than one year from such date.

(g) Though no national bank is authorized under the provisions of section 24 to make a loan on the security of real estate, other than farm land, for a period exceeding one year, nevertheless, at the end of the year, it may properly make a new loan upon the same security for a period not exceeding one year. The maturing note must be canceled and a new note taken in its place, but in order to obviate the necessity of making a new mortgage or deed of trust for each renewal the original mortgage or deed of trust may be so drawn in the first instance as to cover possible future renewals of the original note. Under no circumstances, however, must the bank obligate itself in advance to make such a renewal. It must, in all cases, preserve the right to require payment at the end of the year and to foreclose the mortgage should that action become necessary. The same principles apply to loans of longer maturities secured by farm lands.

(h) In order that real estate loans held by a bank may be readily classified, a statement signed by the officers making a loan and having knowledge of the facts upon which it is based must be attached to each note secured by a first mortgage on the land by which the loan is secured, certifying in detail as of the date of the loan that all of the requirements of law have been duly observed.

REGULATION H.
SERIES OF 1917.
(Superseding Regulation H of 1916.)

MEMBERSHIP OF STATE BANKS AND TRUST COMPANIES.

I. Statutory requirements.

Section 9 of the Federal reserve act, as amended by the act approved June 21, 1917, which authorizes State banks and trust companies to become members of the Federal reserve system, is quoted in the appendix to this regulation on page 24.

II. Banks eligible for membership.

A State bank or a trust company to be eligible for membership in a Federal reserve bank must comply with the following conditions:

1. It must have been incorporated under a special or general law of the State or district in which it is located.
2. It must have a minimum paid-up unimpaired capital stock as follows:
 - In cities or towns not exceeding 3,000 inhabitants, \$25,000.
 - In cities or towns exceeding 3,000 but not exceeding 6,000 inhabitants, \$50,000.
 - In cities or towns exceeding 6,000 but not exceeding 50,000 inhabitants, \$100,000.
 - In cities exceeding 50,000 inhabitants, \$200,000.

III. Application for membership.

Any eligible State bank or trust company may make application on F. R. B. Form 83a, made a part of this regulation, to the Federal Reserve Board for an amount of capital stock in the Federal reserve bank of its district equal to 6 per cent of the paid-up capital stock and surplus of such State bank or trust company. This application must be forwarded direct to the Federal reserve agent of the district in which the applying bank or trust company is located and must be accompanied by Exhibits I, II, and III, referred to on page 1 of the application blank.

IV. Approval of application.

In passing upon an application the Federal Reserve Board will consider especially—

1. The financial condition of the applying bank or trust company and the general character of its management.
2. Whether the corporate powers exercised by the applying bank or trust company are consistent with the purposes of the Federal reserve act.
3. Whether the laws of the State or district in which the applying bank or trust company is located contain provisions likely to prevent proper compliance with the provisions of the Federal reserve act and the regulations of the Federal Reserve Board made in conformity therewith.

If, in the judgment of the Federal Reserve Board, an applying bank or trust company conforms to all the requirements of the Federal reserve act and these regulations, and is otherwise qualified for membership, the board will issue a certificate of approval subject to such conditions as it may deem necessary to insure compliance with the act and these regulations. When the conditions imposed by the board have been accepted by the applying bank or trust company the board will issue a certificate of approval, whereupon the applying bank or trust company shall make a payment to the Federal reserve bank of its district of one-half of the amount of its subscription, i. e., 3 per cent of the amount of its paid-up capital and surplus, and upon receipt of this payment the appropriate certificate of stock will be issued by the Federal reserve bank. The remaining half of the subscription of the applying bank or trust company shall be subject to call when deemed necessary by the Federal Reserve Board.

V. Powers and restrictions.

Every State bank or trust company while a member of the Federal reserve system—

1. Shall retain its full charter and statutory rights as a State bank or trust company, subject to the provisions of the Federal reserve act and to the regulations of the Federal Reserve Board, including any conditions embodied in the certificate of approval.
2. Shall maintain such improvements and changes in its banking practice as may have been specifically required of it by the Federal Reserve Board as a condition of its admission and shall not lower the standard of banking then required of it; and
3. Shall enjoy all the privileges and observe all those requirements of the Federal reserve act and of the regulations of the Federal Reserve Board made in conformity therewith which are applicable to State banks and trust companies which have become member banks.

VI. *Examinations and reports.*

Every State bank or trust company, while a member of the Federal reserve system, shall be subject to examinations made by direction of the Federal Reserve Board or of the Federal reserve bank by examiners selected or approved by the Federal Reserve Board.

In order to avoid duplication, examinations of State banks and trust companies made by State authorities will be accepted in lieu of examinations by examiners selected or approved by the board wherever these are satisfactory to the directors of the Federal reserve bank and where, in addition, satisfactory arrangements for cooperation in the matter of examination between the designated examiners of the board and those of the States already exist or can be effected with State authorities. Examiners from the staff of the board or of the Federal reserve banks will, whenever desirable, be designated by the board to act with the examination staff of the State in order that uniformity in the standard of examination may be assured.

Every State bank or trust company, while a member of the Federal reserve system, shall be required to make in each year not less than three reports of condition and of the payment of dividends. Such reports shall be made to the Federal reserve bank of its district on call of such bank on dates to be fixed by the Federal Reserve Board.

REGULATION I.
SERIES OF 1917.
(Superseding Regulation I of 1916.)

INCREASE OR DECREASE OF CAPITAL STOCK OF FEDERAL RESERVE BANKS.

INCREASE OF CAPITAL STOCK.

Whenever the capital stock of any Federal reserve bank shall be increased by new banks becoming members, or by the increase of capital or surplus of any member bank and the allotment of additional capital stock to such bank, the board of directors of such Federal reserve bank shall certify such increase to the Comptroller of the Currency on Form 58, which is made a part of this regulation.

DECREASE OF CAPITAL STOCK.

I. Whenever a member bank reduces its capital stock or surplus, and, in the case of reduction of its capital, such reduction has been approved by the Comptroller of the Currency and by the Federal Reserve Board in accordance with the provisions of section 23 of the Federal reserve act, it shall file with the Federal reserve bank of which it is a member an application on Form 60, which is made a part of this regulation. When this application has been approved, the Federal reserve bank shall take up and cancel the receipt issued to such bank for cash payments made on its subscription and shall issue in lieu thereof a new receipt after refunding to the member bank the proportionate amount due such bank on account of the subscription canceled. The receipt so issued shall show the date of original issue, so that dividends may be calculated thereon.

II. Whenever a member bank shall be declared insolvent and a receiver appointed by the proper authorities, such receiver shall file with the Federal reserve bank of which the insolvent bank is a member an application on Form 87, which is made a part of this regulation, for the surrender and cancellation of the stock held by, and for the refund of all balances due to such insolvent member bank. Upon approval of this application by the Federal reserve agent the Federal reserve bank shall accept and cancel the stock surrendered, and shall adjust accounts between the member bank and the Federal reserve bank by applying to the indebtedness of the insolvent member bank to such Federal reserve bank all cash-paid subscriptions made by it on the stock canceled with one-half of 1 per cent per month from the period of last dividend, if earned, not to exceed the book value thereof, and the balance, if any, shall be paid to the duly authorized receiver of such insolvent member bank.

III. Whenever a member bank goes into voluntary liquidation and a liquidating agent is appointed, such agent shall file with the Federal reserve bank of which it is a member an application on Form 86, which is made a part of this regulation, for the surrender and cancellation of the stock held by and for the refund of all balances due to such liquidating member bank. Upon approval of this application by the Federal reserve agent the Federal reserve bank shall accept and cancel the stock surrendered, and shall adjust accounts between the liquidating member bank and the

Federal reserve bank by applying to the indebtedness of the liquidating member bank to such Federal reserve bank all cash-paid subscriptions made by it on the stock canceled with one-half of 1 per cent per month from the period of last dividend, if earned, not to exceed the book value thereof, and the balance, if any, shall be paid to the duly authorized liquidating agent of such liquidating member bank.

IV. Whenever the stock of a Federal reserve bank shall be reduced in the manner provided in Paragraphs I, II, or III of this regulation the board of directors of such Federal reserve bank shall, in accordance with the provisions of section 6, file with the Comptroller of the Currency a certificate of such reduction on Form 59, which is made a part of this regulation.

REGULATION J.
SERIES OF 1917.
(Superseding Regulation J of 1916.)

CHECK CLEARING AND COLLECTION.

Section 16 of the Federal reserve act authorizes the Federal Reserve Board to require each Federal reserve bank to exercise the function of a clearing house for its member banks, and section 13 of the Federal reserve act, as amended by the act approved June 21, 1917, authorizes each Federal reserve bank to receive from any nonmember bank or trust company, solely for the purposes of exchange or of collection, deposits of current funds in lawful money, national-bank notes, Federal reserve notes, checks, and drafts payable upon presentation, or maturing notes and bills, provided such nonmember bank or trust company maintains with its Federal reserve bank a balance sufficient to offset the items in transit held for its account by the Federal reserve bank.

In pursuance of the authority vested in it under these provisions of law, the Federal Reserve Board, desiring to afford both to the public and to the various banks of the country a direct, expeditious, and economical system of check collection and settlement of balances, has arranged to have each Federal reserve bank exercise the functions of a clearing house for such of its member banks as desire to avail themselves of its privileges and for such State banks and trust companies as may maintain with the Federal reserve bank a balance sufficient to qualify it as a clearing member under the provisions of section 13.

Each Federal reserve bank shall exercise the functions of a clearing house under the following general terms and conditions:

(1) Each Federal reserve bank will receive at par from its member banks and from nonmember banks in its district which have become clearing members, checks¹ drawn on all member and clearing member banks and on all other nonmember banks which agree to remit at par through the Federal reserve bank of their district.

(2) Each Federal reserve bank will receive at par from other Federal reserve banks and will receive at par from all member and clearing member banks, regardless of their location, for the credit of their accounts with their respective Federal reserve banks, checks drawn upon all member and clearing member banks of its district and upon all other nonmember banks of its district whose checks can be collected at par by the Federal reserve bank. 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 and clearing member banks.

(3) 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 part of the minimum reserve nor become available to meet checks drawn until actually collected, in accordance with the best practice now prevailing.

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

(5) In the selection of collecting agents for handling checks on nonmember banks, which have not become clearing members, member banks will be given the preference.

(6) Under this plan each Federal reserve bank will receive at par from its member and clearing member banks checks on all member and clearing member banks and on all other nonmember banks whose checks can be collected at par by any Federal reserve bank. Member and clearing member banks will be required by the Federal

¹ A check is generally defined as a draft or order upon a bank or order upon a bank or banking house purporting to be drawn upon a deposit of funds, for the payment at all events of a certain sum of money to a certain person therein named, or to him or his order, or to bearer, and payable instantly on demand.

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 or clearing member bank may ship currency or specie 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.¹

(7) Section 19 of the Federal reserve act provides that—

“The required balance 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 balance required by law is fully restored.”

It is manifest that items in process of collection can not lawfully be counted as part of the minimum reserve balance to be carried by a member bank with its Federal reserve bank. Therefore, should a member bank draw against such items the draft would be charged against its reserve balance if such balance were sufficient in amount to pay it; but any resulting impairment of reserve balances would be subject to all the penalties provided by the act.

Inasmuch as it is essential that the law in respect to the maintenance by member banks of the required minimum reserve balance shall be strictly complied with, the Federal Reserve Board, under authority vested in it by section 19 of the act, hereby prescribes as the penalty for any deficiency in reserves a sum equivalent to an interest charge on the amount of the deficiency of 2 per cent per annum above the 90 day discount rate of the Federal reserve bank of the district in which the member bank is located. The board reserves the right to increase this penalty whenever conditions require it.

For the purpose of keeping their reserve balances intact member banks may at all times have recourse to the rediscount facilities offered by their respective Federal reserve banks.

(8) 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 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.

(9) In handling items for member and clearing member banks, a Federal reserve bank will act as agent only. The board will require that each member and clearing member bank authorize its Federal reserve bank to send checks for collection to banks on which checks are drawn, and, except for negligence, such Federal reserve bank 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 and clearing member banks. Each Federal reserve bank will also promulgate rules and regulations governing the details of its operations as a clearing house, such rules and regulations to be binding upon all member and nonmember banks which are clearing through the Federal reserve bank.

(10) 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.

¹In accordance with instructions issued by the Federal Reserve Board on Apr. 24, 1917, the various Federal reserve banks have issued circulars setting forth the conditions under which their respective member banks may draw drafts on their reserve bank accounts payable with or through any other Federal reserve bank.

STATE BANKS IN FEDERAL RESERVE SYSTEM.

APPENDICES.

APPENDIX TO REGULATION E (P. 11).

“NET FUNDED INDEBTEDNESS.”

The term “net funded indebtedness” is hereby defined to mean the legal gross indebtedness of the municipality (including the amount of any school district or other bonds which depend for their redemption upon taxes levied upon property within the municipality) less the aggregate of the following items:

- (1) The amount of outstanding bonds or other debt obligations made payable from current revenues;
- (2) The amount of outstanding bonds issued for the purpose of providing the inhabitants of a municipality with public utilities, such as waterworks, docks, electric plants, transportation facilities, etc.: *Provided*, That evidence is submitted showing that the income from such utilities is sufficient for maintenance, for payment of interest on such bonds, and for the accumulation of a sinking fund for their redemption;
- (3) The amount of outstanding improvement bonds, issued under laws which provide for the levying of special assessments against abutting property in amounts sufficient to insure the payment of interest on the bonds and the redemption thereof: *Provided*, That such bonds are direct obligations of the municipality and included in the gross indebtedness of the municipality;
- (4) The total of all sinking funds accumulated for the redemption of the gross indebtedness of the municipality, except sinking funds applicable to bonds just described in (1), (2), and (3) above.

“EXISTENCE” AND “NONDEFAULT.”

Warrants will be construed to comply with that part of I (c) of Regulation E relative to terms of existence and nondefault, under the following conditions:

(1) Warrants issued by or in behalf of any municipality which was, subsequent to the issuance of such warrants, consolidated with or merged into an existing political division which meets the requirements of these regulations, will be deemed to be the warrants of such political division: *Provided*, That such warrants were assumed by such political division under statutes and appropriate proceedings the effect of which is to make such warrants general obligations of such assuming political division and payable, either directly or ultimately, without limitation to a special fund from the proceeds of taxes levied upon all the taxable real and personal property within its territorial limits.

(2) Warrants issued by or in behalf of any municipality which was, subsequent to the issuance of such warrants, wholly succeeded by a newly organized political division whose term of existence, added to that of such original political division or of any other political division so succeeded, is equal to a period of 10 years will be deemed to be warrants of such succeeding political division: *Provided*, That during such period none of such political divisions shall have defaulted for a period exceeding 15 days in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it: *And provided further*, That such warrants were assumed by such new political division under statutes and appropriate proceedings the effect of which is to make such warrants general obligations of such assuming political division and payable, either directly or ultimately, without limitation to a special fund from the proceeds of taxes levied upon all the taxable real and personal property within its territorial limits.

(3) Warrants issued by or in behalf of any municipality which, prior to such issuance, became the successor of one or more, or was formed by the consolidation or merger of two or more, preexisting political divisions, the term of existence of one or more of which, added to that of such succeeding or consolidated political division, is equal to a period of 10 years, will be deemed to be warrants of a political division which has been in existence for a period of 10 years: *Provided*, That during such period none of such original, succeeding, or consolidated political divisions shall have defaulted for a period exceeding 15 days in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it.

APPENDIX TO REGULATION H (P. 17).

Section 9 of the Federal reserve act as amended by the act approved June 21, 1917, provides that:

Any bank incorporated by special law of any State, or organized under the general laws of any State, or of the United States, desiring to become a member of the Federal reserve system, may make application to the Federal Reserve Board, under such rules and regulations as it may prescribe, for the right to subscribe to the stock of the Federal reserve bank organized within the district in which the applying bank is located. Such application shall be for the same amount of stock that the applying bank would be required to subscribe to as a national bank. The Federal Reserve Board, subject to such conditions as it may prescribe, may permit the applying bank to become a stockholder of such Federal reserve bank.

In acting upon such applications the Federal Reserve Board shall consider the financial condition of the applying bank, the general character of its management, and whether or not the corporate powers exercised are consistent with the purposes of this act.

Whenever the Federal Reserve Board shall permit the applying bank to become a stockholder in the Federal reserve bank of the district, its stock subscription shall be payable on call of the Federal Reserve Board, and stock issued to it shall be held subject to the provisions of this act.

All banks admitted to membership under authority of this section shall be required to comply with the reserve and capital requirements of this act and to conform to those provisions of law imposed on national banks which prohibit such banks from lending on or purchasing their own stock, which relate to the withdrawal or impairment of their capital stock, and which relate to the payment of unearned dividends. Such banks and the officers, agents, and employees thereof shall also be subject to the provisions of and to the penalties prescribed by section 5209 of the Revised Statutes, and shall be required to make reports of condition and of the payment of dividends to the Federal reserve bank of which they become a member. Not less than three of such reports shall be made annually on call of the Federal reserve bank on dates to be fixed by the Federal Reserve Board. Failure to make such reports within 10 days after the date they are called for shall subject the offending bank to a penalty of \$100 a day for each day that it fails to transmit such report; such penalty to be collected by the Federal reserve bank by suit or otherwise.

As a condition of membership such banks shall likewise be subject to examinations made by direction of the Federal Reserve Board or of the Federal reserve bank by examiners selected or approved by the Federal Reserve Board.

Whenever the directors of the Federal reserve bank shall approve the examinations made by the State authorities, such examinations and the reports thereof may be accepted in lieu of examinations made by examiners selected or approved by the Federal Reserve Board: *Provided, however,* That when it deems it necessary the board may order special examinations by examiners of its own selection and shall in all cases approve the form of report. The expenses of all examinations, other than those made by State authorities, shall be assessed against and paid by the banks examined.

If at any time it shall appear to the Federal Reserve Board that a member bank has failed to comply with the provisions of this section or the regulations of the Federal Reserve Board made pursuant thereto, it shall be within the power of the board after hearing to require such bank to surrender its stock in the Federal reserve bank and to forfeit all rights and privileges of membership. The Federal Reserve Board may restore membership upon due proof of compliance with the conditions imposed by this section.

Any State bank or trust company desiring to withdraw from membership in a Federal reserve bank may do so, after six months' written notice shall have been filed with the Federal Reserve Board, upon the surrender and cancellation of all of its holdings of capital stock in the Federal reserve bank: *Provided, however,* That no Federal reserve bank shall, except under express authority of the Federal Reserve Board, cancel within the same calendar year more than 25 per cent of its capital stock for the purpose of effecting voluntary withdrawals during that year. All such applications shall be dealt with in the order in which they are filed with the board.

Whenever a member bank shall surrender its stock holdings in a Federal reserve bank, or shall be ordered to do so by the Federal Reserve Board, under authority of law, all of its rights and privileges as a member bank shall thereupon cease and determine, and after due provision has been made for any indebtedness due or to become due to the Federal reserve bank it shall be entitled to a refund of its cash paid subscription with interest at the rate of one-half of 1 per cent per month from date of last dividend, if earned, the amount refunded in no event to exceed the

book value of the stock at that time, and shall likewise be entitled to repayment of deposits and of any other balance due from the Federal reserve bank.

No applying bank shall be admitted to membership in a Federal reserve bank unless it possesses a paid-up unimpaired capital sufficient to entitle it to become a national banking association in the place where it is situated under the provisions of the national bank act.

Banks becoming members of the Federal reserve system under authority of this section shall be subject to the provisions of this section and to those of this act which relate specifically to member banks, but shall not be subject to examination under the provisions of the first two paragraphs of section 5240 of the Revised Statutes as amended by section 21 of this act. Subject to the provisions of this act and to the regulations of the board made pursuant thereto, any bank becoming a member of the Federal reserve system shall retain its full charter and statutory rights as a State bank or trust company, and may continue to exercise all corporate powers granted it by the State in which it was created, and shall be entitled to all privileges of member banks: *Provided, however,* That no Federal reserve bank shall be permitted to discount for any State bank or trust company notes, drafts, or bills of exchange of any one borrower who is liable for borrowed money to such State bank or trust company in an amount greater than 10 per cent of the capita and surplus of such State bank or trust company, but the discount of bills of exchange drawn against actually existing value and the discount of commercial or business paper actually owned by the person negotiating the same shall not be considered as borrowed money within the meaning of this section. The Federal reserve bank, as a condition of the discount of notes, drafts, and bills of exchange for such State bank or trust company, shall require a certificate or guaranty to the effect that the borrower is not liable to such bank in excess of the amount provided by this section, and will not be permitted to become liable in excess of this amount while such notes, drafts, or bills of exchange are under discount with the Federal reserve bank.

It shall be unlawful for any officer, clerk, or agent of any bank admitted to membership under authority of this section to certify any check drawn upon such bank unless the person or company drawing the check has on deposit therewith at the time such check is certified an amount of money equal to the amount specified in such check. Any check so certified by duly authorized officers shall be a good and valid obligation against such bank, but the act of any such officer, clerk, or agent in violation of this section may subject such bank to a forfeiture of its membership in the Federal Reserve System upon hearing by the Federal Reserve Board.

EXHIBIT D.

MARCH 21, 1918.

SIR: You have requested my opinion as to whether the limitations contained in section 13 of the Federal reserve act relating to charges for the collection and payment of checks can be held to apply to State banks which are neither members of the Federal Reserve System nor depositors in Federal reserve banks.

As originally enacted, the first paragraph of section 13 reads as follows:

"Any Federal reserve bank may receive from any of its member banks, and from the United States, deposits of current funds in lawful money, national-bank notes, Federal reserve notes, or checks and drafts upon solvent member banks, payable upon presentation, or, solely for exchange purposes, may receive from other Federal reserve banks deposits of current funds in lawful money, national-bank notes, or checks and drafts upon solvent member or other Federal reserve banks, payable upon presentation."

In section 16, apparently as the basis of a system of check clearing or collection, it is provided that Federal reserve banks *shall receive on deposit at par checks and drafts on member and other Federal reserve banks*; and the Federal Reserve Board is authorized to fix by rule the charges to be collected by member banks from patrons whose checks are cleared through the Federal reserve bank any charge for the service of clearing or collection rendered by the Federal reserve bank.

It will be noted that under the first paragraph of section 13 in its original form the only classes of banks which might be depositors in and thus clear through a Federal reserve bank were its member banks and other Federal reserve banks, and the only checks and drafts specified as receivable on deposit were checks and drafts drawn upon member banks or upon other Federal reserve banks.

The acts of September 7, 1916, and June 21, 1917, so amended the first paragraph of section 13 as to extend the clearing and collection facilities of the Federal Reserve System to include checks and drafts generally, to make these facilities directly available to nonmember banks, and to establish the limitations as to charges referred to in the question submitted. The paragraph as so amended reads as follows:

"Any Federal reserve bank may receive from any of its member banks, and from the United States, deposits of current funds in lawful money, national-bank notes, Federal reserve notes, or checks and drafts, payable upon presentation, and also, for collection, maturing notes and bills; or, solely for purposes of exchange or of collection, may receive from other Federal reserve banks deposits of current funds in lawful money, national-bank notes, or checks upon other Federal reserve banks, and checks and drafts, payable upon presentation within its district, and maturing notes and bills payable within its district; or, solely for the purposes of exchange or of collection, may receive from any nonmember bank or trust company deposits of current funds in lawful money, national-bank notes, Federal reserve notes, checks, and drafts payable upon presentation, or maturing notes and bills: *Provided*, Such nonmember bank or trust company maintains with the Federal reserve bank of its district a balance sufficient to offset the items in transit held for its account by the Federal reserve bank: *Provided further*, That nothing in this or any other section of this act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per \$100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise; but no such charges shall be made against the Federal reserve banks." [Italics mine.]

The limitations as to charges referred to in the question submitted are contained in the second proviso quoted above. This proviso, apparently recognizing an existing right of member and nonmember banks to make reasonable charges for the collection or payment of checks and drafts and remission therefor by exchange or otherwise provides (1) that these charges are "to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per \$100," but (2) that "no such charges shall be made against the Federal reserve banks."

Clearly these limitations apply to national banks, which are compelled to be member banks, to such State banks as become member banks by voluntarily accepting the terms and provisions of the Federal reserve act, and to such other State banks as do not become member banks but by becoming depositors in Federal reserve banks upon the conditions specified avail themselves directly of the facilities of the Federal reserve clearing system.

The specific question to be determined is whether these limitations apply to nonmember State banks which do not become depositors but checks upon which may pass through Federal reserve banks in process of clearing or collection.

The theory and scheme of the Federal reserve legislation seems inconsistent with the purpose on the part of Congress to subject State banks *against their will* to Federal control or regulation. State banks are not compelled to become members of the Federal reserve system or depositors therein. Those possessing the necessary qualifications are, however, invited to become members. They are not only free to accept or decline, but if they accept remain at liberty to withdraw from the system. (Sec. 9.) By section 13 as amended, State banks not desiring to become members or too small to be eligible for membership are likewise *invited* to share in the clearing and collection facilities of the system by becoming depositors in Federal reserve banks. But they may accept or reject the invitation, and if they become depositors may close their accounts at their pleasure.

It would accordingly seem that the limitations referred to ought not to be regarded as intended to be imposed upon State banks not connected with the Federal reserve system as members or depositors, against the will of such banks, unless that intention clearly appears.

The term "nonmember bank" as used in the proviso may reasonably be construed as referring to a nonmember bank that has become a depositor as authorized in the preceding provisions of the paragraph. If this term is so construed, obviously the provision requiring charges "to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per \$100," will have no application to nonmember State banks which are not depositors in a Federal reserve bank. The broad language of the concluding clause, "no such charges shall be made against the Federal reserve banks," may be construed not as directed against State banks which are not depositors, but merely as specifying a condition upon which checks may clear through the Federal reserve banks—in effect a prohibition against the payment of such charges by the Federal reserve banks.

Under this construction, member banks and nonmember banks which are depositors in the Federal reserve banks will be subject to the limitations in the proviso, but nonmember banks which are not depositors will not be subject to the limitations. All, however, will have to adjust their charges among themselves and with their own depositors, the Federal reserve banks being prohibited from paying such charges.

This construction seems to be in harmony with the intention of the framers of the amendment to section 13 embodying the above-mentioned proviso.

The act of June 21, 1917, amending section 13 and other sections of the Federal reserve act, as originally introduced in both the House and Senate contained no part of the (second) proviso, the section in the proposed amended form ending with the preceding proviso. The Senate, adopting an amendment offered by Senator Hardwick, added the second proviso in the following form:

"*Provided further*, That nothing in this or any other section of this act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, but in no case to exceed 10 cents per \$100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise." (55 Cong. Rec., 2065.)

It was thought the effect of the Hardwick amendment would be to recognize the right of any bank upon which checks are drawn to make charges against the Federal reserve bank through which such checks might be cleared or collected. The Hardwick amendment was opposed by the Federal Reserve Board, as appears from letters from its governor to Senator Owen and Congressman Glass, chairmen of the respective Committees on Banking and Currency of the Senate and House (pp. 2071, 3795). The President also called attention to the seeming effect of the amendment in a letter to Senator Owen, reading as follows:

"I have been a good deal disturbed to learn of the proposed amendment to the Federal reserve act which seems to contemplate *charging the Federal reserve banks for payment of checks cleared by them*, or charging the payee of such checks passing through the reserve banks with a commission. I should regard such a provision as most unfortunate and as almost destructive of the function of the Federal reserve banks as a clearing house for member banks, a function which they have performed with so much benefit to the business of the country.

"I hope most sincerely that this matter may be adjusted without interfering with this indispensable clearing function of the banks" (p. 4083).

In conference, apparently as the result of the letters of the governor of the Federal Reserve Board and the President, the proviso took its present form, two changes being made by the conferees: First, the charges which member or nonmember banks may make were made subject "to be determined and regulated by the Federal Reserve Board"; and, second, the final clause was added, "but no such charges shall be made against the Federal reserve banks."

In presenting the conference report to the Senate, Senator Owen emphasized the importance of not interfering with the clearing functions of the Federal reserve banks, explained that under the proviso as amended "the banks can charge each other for making these accommodations if they like, and they can adjust that to their own satisfaction with one another without troubling the reserve banks," and apparently conceded that State banks not connected as members or depositors with the Federal Reserve System could not be subjected to Federal legislation (p. 4083).

Mr. Glass in presenting the report to the House, said:

"The Congress has no control whatsoever over nonmember banks. It can not regulate their charges and will not regulate them if this Hardwick amendment should prevail. * * * This House has no control over the nonmember bank in this matter. Even the Federal Reserve Board has no control over their operations unless they voluntarily join the voluntary collection system established by the Federal Reserve Board" (p. 3794).

And further, "no nonmember bank that does not voluntarily join the collection system established by the Federal Reserve Board will be specifically affected. No law that we pass here can directly affect them. The only way they can be affected is incidental" (p. 3795).

It thus seems clear that the proviso was understood by Congress as designed to protect the clearing functions of the Federal reserve banks and not directed at State banks which have no connection as members or depositors with the Federal Reserve System and upon which it was considered the effect of the proviso could be only incidental.

It may be argued, and is probably true, that the proviso will necessarily affect the practice of State banks, though not members or depositors, as to making charges for the payment of checks drawn upon them. With the concentration of reserve balances in Federal reserve banks as required by the Federal reserve act, the Federal reserve clearing system may offer the only adequate and convenient facilities for clearing or collecting checks drawn upon banks at a distance, and depositors may find it inadvisable to maintain accounts with banks upon which checks can not be cleared or collected by the use of these facilities.

The Federal reserve act, however, does not command or compel these State banks to forego any right they may have under the State laws to make charges in connection with the payment of checks drawn upon them. The act merely offers the clearing and collection facilities of the Federal reserve banks upon specified conditions. If the State banks refuse to comply with the conditions by insisting upon making charges against the Federal reserve banks, the result will simply be, so far as the Federal reserve act is concerned, that since the Federal reserve banks can not pay these charges they can not clear or collect checks on banks demanding such payment from them.

From what has been said it follows that in my opinion the limitations contained in section 13 relating to charges for the collection and payment of checks do not apply to State banks not connected with the Federal Reserve System as members or depositors. Checks on banks making such charges can not, however, be cleared or collected through Federal reserve banks.

Respectfully,

(Signed) T. W. GREGORY, *Attorney General*.

The PRESIDENT,
The White House.

EXHIBIT E.

APRIL 30, 1918.

MY DEAR GOVERNOR: I acknowledge receipt of your letter of the 19th instant with reference to my opinion of March 21, 1918, holding that Federal reserve banks are prohibited from paying the charges for collection and payment of checks and drafts mentioned in the first paragraph of section 13 of the Federal reserve act.

In a memorandum by the general counsel of the American Bankers Association, which you inclose, the point is raised that the prohibition against the charges referred to must be confined to checks owned by the Federal reserve bank as distinguished from checks deposited to be cleared or collected for the account of a member or depositor.

You ask to be advised whether the board correctly interprets my opinion as implying that no such distinction can be recognized and that no member bank can under any circumstances make any charge against its Federal reserve bank in connection with the collection or payment of checks deposited with the Federal reserve bank as provided in the paragraph mentioned.

The reason for the suggested distinction is not apparent. I do not understand why checks deposited with a Federal reserve bank to be cleared or collected can not be considered as owned by the bank.

As the basis of the check-clearing system contemplated by the Federal reserve act, the Federal reserve banks are required by section 16 to "receive on deposit at par," unconditionally, the checks therein specified drawn on Federal reserve and member banks. If the phrase "receive on deposit" is given its ordinary signification, it seems clear that the Federal reserve bank becomes the owner of the checks so deposited, title to the checks passing to that bank and the depositors receiving immediate credit therefor. (*Burton v. United States*, 196 U. S., 283; *Security National Bank v. Old National Bank*, 241 Fed. 1, and cases therein cited at pages 10 to 12.)

The first paragraph of section 13, as amended to extend the clearing facilities of the Federal reserve banks to nonmember banks and to include checks generally, requires each nonmember bank availing itself of these facilities to maintain with the "Federal reserve bank of its district a balance sufficient to offset the items in transit held by the Federal reserve bank." As so amended, the paragraph may be regarded as at least authorizing the Federal reserve bank to receive on deposit from nonmember depositors as well as from member banks all classes of checks to be cleared or collected, taking the title thereto and giving credit therefor to the depositing banks.

As a Federal reserve bank may thus become the owner of all the checks cleared or collected through it, there appears to be no basis in the act for drawing a distinction between checks owned by the Federal reserve bank and checks deposited with it to be cleared or collected.

But even if the checks received could be classified on the basis suggested, the language of the paragraph seems to preclude the idea of excluding checks deposited to be cleared or collected from the checks as to which charges are prohibited.

The charges which the Federal reserve banks are prohibited from paying by the final clause, "no such charges shall be made against the Federal reserve banks," obviously include the "charges * * * for collection or payment of checks and drafts and remission therefor by exchange or otherwise" mentioned in the preceding clause. The checks authorized by the paragraph to be deposited with the Federal reserve bank, upon being received by that bank, are to be collected from and paid by the banks upon which they are drawn. To say that charges in connection with the pay-

ment of these checks made by the banks drawn upon and collected from the Federal reserve bank are not made against that bank seems to do violence to the ordinary meaning of the words used, regardless of whether the charges are ultimately borne by it or subsequently transferred to the banks by which the checks were deposited.

Moreover, the legislative history of the amendment as referred to in the opinion shows clearly that the prohibition was directed primarily against the making of charges in connection with the clearing of checks. It was a proposed amendment to the Federal reserve act, which apparently contemplated "charging the Federal reserve banks for payment of checks cleared by them" that the President opposed in his letter to Senator Owen. And it was to prevent the possibility of such charges being made that the final clause was added, which, as explained by Senator Owen, prevented "troubling the reserve banks" or "interfering with the clearing of checks at par by the reserve banks." (55 Cong. Rec., p. 3761.)

I construe the first paragraph of section 13 as prohibiting member banks under any circumstances from making the charges therein referred to against Federal reserve banks.

You are accordingly advised that the interpretation placed by the board upon my opinion of March 21 is correct.

Respectfully,

(Signed)

T. W. GREGORY,
Attorney General.

Hon. W. P. G. HARDING,
Governor Federal Reserve Board, Washington, D. C.

EXHIBIT F.

FEDERAL RESERVE BOARD,
Washington, December 11, 1919.

Subject: Questions of law and policy involved in matter of collecting all checks at par.

DEAR SIR: In view of complaints which are being made from time to time concerning the policy of Federal reserve banks in collecting checks on all points in their respective districts at par, there is inclosed for your information a copy of a letter which was sent to a protesting nonmember bank in one of the districts, which defines the questions of law and policy involved.

Very truly, yours,

GOVERNOR.

TO CHAIRMEN AND GOVERNORS OF ALL FEDERAL RESERVE BANKS.

DEAR SIR: Receipt is acknowledged of your letter of the ——— in which you protest against the policy which has been adopted by the Federal reserve banks with the approval of the Federal Reserve Board in the matter of the collection of checks which are received by Federal reserve banks from their member banks or from nonmember banks which maintain clearing or collection accounts with them.

The board's action is based upon its conception of the very evident purposes of the Federal reserve act. Section 13 of the act begins as follows: "Any Federal reserve bank may receive from any of its member banks, and from the United States, deposits of current funds in lawful money, national bank notes, Federal reserve notes, or checks, and drafts, payable upon presentation, and also, for collection, maturing notes and bills." Even though the Federal Reserve Board has heretofore ruled that the permissive "may," as used in the foregoing paragraph, should not be construed to mean the mandatory "shall," nevertheless it is clear that a Federal reserve bank in order to do any business whatever must exercise some of the permissive powers authorized by law. It would be impossible otherwise for a Federal reserve bank to afford to its member banks many of the privileges which the law clearly contemplates and to which the member banks are clearly entitled. But, independently of a discussion of this phase of the situation, it seems to the board that doubts upon this question are resolved upon a consideration of the provisions of section 16. "Every Federal reserve bank shall receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors." In this case, the obligatory "shall" is used so that there is no option in the Federal reserve bank so far as checks and drafts upon its depositors are concerned. From this it may be argued that as the depositors of a Federal reserve bank are member banks there is no call obligation upon the Federal reserve bank to receive on deposit at par checks on nonmember banks, but even if the language of section 13 be construed as per-

missive there seems to be no question that the Federal reserve bank has the right to receive on deposit from any of its member banks any checks or drafts upon whomsoever drawn, provided they are payable upon presentation. The whole purpose of the act demands that in justice to member banks, they should exercise that right.

Section 16 further provides that the Federal Reserve Board "may, at its discretion, exercise the functions of a clearing house for such Federal reserve banks * * * and may also require each such bank to exercise the functions of a clearing house for its member banks." In accordance with the purpose of this paragraph, the Federal Reserve Board, with the view ultimately of establishing a universal or national system of clearing intersectional balances as well as bank checks and drafts, has established a gold settlement fund through which daily clearings between all Federal reserve banks are consummated and has also required each Federal reserve bank to exercise the functions of a clearing house for its member banks. In order, however, to make fully effective its facilities as a clearing house in accordance with the terms of this section, there does not seem to be any doubt that the Federal reserve bank should not only exercise its obligatory power to receive from member banks checks and drafts drawn upon other member banks, but that it should also exercise its permissive power to receive from member banks any other checks and drafts upon whomsoever drawn, provided that they are payable upon presentation.

There are no doubt many nonmember banks without sufficient capitalization to make them eligible for membership in the Federal reserve system, but provision is made for such banks in section 13 by authorizing the Federal reserve banks, for purposes of exchange or of collection, to receive deposits from any nonmember bank or trust company. But for the fact that the small country banks are able to have their out-of-town items credited at par by some city correspondent, there is no doubt that many more of them would avail themselves of the nonmember collection privilege than have done so.

There is a proviso in section 13 which allows member and nonmember banks to make reasonable charges "to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per \$100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts, and remission thereof by exchange or otherwise; but no such charges shall be made against the Federal reserve banks."¹⁷ This has been construed by the Attorney General of the United States as meaning that a Federal reserve bank can not legally pay any fee to a member or nonmember bank for the collection and remittance of a check. It follows, therefore, that if the Federal reserve banks are to give the service required of them under the provisions of section 13 they must, in cases where banks refuse to remit for their checks at par, use some other means of collection no matter how expensive.

The action of the various Federal reserve banks in extending their par lists has met with the cordial approval of the Federal Reserve Board, which holds the view that under the terms of existing law, the Federal reserve banks must use every effort to collect all bank checks received from member banks at par. Several of the Federal reserve banks are now able to collect on all points in their respective districts at par, and new additions to the other par lists are being made every day. The board sees no objection to one bank charging another bank or a firm or individual the full amount provided in section 13 of the Federal reserve act (10 cents per \$100), and has not undertaken to modify these charges, but the act expressly provides that no such charge shall be made against the Federal reserve banks.

It is the board's duty to see that the law is administered fairly and without discrimination, and that it applies to all banks alike, and it is making an earnest endeavor to carry out the laws as construed by the highest legal authority of the administrative branch of the Government.

EXHIBIT G.

FIRST LETTER TO THE NONMEMBER BANK.

GENTLEMEN: You are doubtless aware of the fact that we have in the past been obliged to refuse to handle checks on your bank for the reason that we have not had a par arrangement with you.

Federal reserve banks can not handle checks on banks under any arrangements which would contemplate the paying of exchange because, under the Attorney General's interpretation of the law, they are not, under any circumstances, permitted to pay exchange.

Our declining to handle checks drawn by your depositors has not in any case been intended as a reflection on your bank and we believe that you have not so considered it.

The campaign conducted by the Federal reserve banks for the addition of new par points has reached such a stage that we do not feel justified in any longer refusing to handle checks on banks located in what we must consider as being par territory.

We would advise, therefore, that on and after November 15, we will discontinue refusing to handle checks on you, but will receive at par such checks as are offered to us and will forward them to you in our regular cash letters, accompanied by stamped, addressed envelopes for such convenience in making returns. Remittance should, in all cases, be made in ——— exchange or its equivalent at par.

We trust that this will meet with your approval and that we may receive your early advice to the effect that we may expect your cooperation in this important movement.

SECOND LETTER TO THE NONMEMBER BANK.

GENTLEMEN: Referring to our letter of November 28, we would say that we are to-day in receipt of checks on you which we have received at par in accordance with the Federal reserve act.

These checks are being forwarded to you to-day in one of our regular cash letters accompanied by stamped, addressed envelope for your convenience in making returns.

We anticipate par remittance in ——— exchange or its equivalent and hope that we may receive your assurance that you will continue to remit at par for all checks drawn by your depositors which we may receive and forward to you in the usual course of business.

THIRD LETTER TO NONMEMBER BANK.

GENTLEMEN: We are in receipt of your remittance covering our cash letter of January 14, total \$1,549.22 and note your deduction of \$2.32 exchange.

Practically all of the banks in ——— have already agreed to remit to us at par for checks drawn by their depositors, received by us and forwarded in the usual course of business and we were hoping that the bank of ———, would also agree to cooperate with us in this important movement.

We can not in justice to the great number of par banks in your vicinity decline to handle checks drawn on you, and since we are not permitted to pay exchange it necessarily follows that we must arrange to collect them at par.

If we can not obtain a direct connection with your good bank, we will be obliged to make collection through other channels.

We request therefore that hereafter if you can not remit at par, you be good enough to certify and return to us such checks as are forwarded to you in our cash letters. ▶

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[Telegram.]

FEDERAL RESERVE BOARD,
Washington, January 20, 1920.

GOVERNOR OF ALL FEDERAL RESERVE BANKS:

Under a resolution adopted by the Senate yesterday Board is required to inform the Senate whether Federal Reserve Board or any Federal reserve bank under instructions or with consent of knowledge of board has resorted to any method of coercion to compel State banks to join Federal reserve system, or by threats or other coercive means has attempted to require such State banks to submit to any rules or regulations made by Federal Reserve Board or any Federal reserve bank. This is result of complaints made to Senators by State banks of efforts of Federal reserve banks to collect checks at par. Specific charge is made that Federal reserve banks hold back checks on small banks until they amount to considerable sums, then send messenger to make personal demand for payment in currency in order to embarrass payee bank and compel it to submit. Has such action been taken by your bank and if so, was it done with object of embarrassing payee bank or merely to reduce percentage cost of collection? Is it not the usual practice of larger banks in your district when they collect on nonmember banks by sending items direct to avail themselves of lower charges by holding back small items until they have round amounts of \$100 or more, thus avoiding payment minimum charge of 10 or 15 cents on a \$5 item? State primary purpose of the use of express companies or private agencies and give outline of any threats, oral or written, which may have been made by your employees or agents. Please wire answer.

HARDING.

EXHIBIT I.

TELEGRAMS FROM THE 12 FEDERAL RESERVE BANKS REPLYING TO THE TELEGRAM OF THE FEDERAL RESERVE BOARD, DATED JANUARY 21, AND MARKED EXHIBIT H.

BOSTON, MASS., *January 21, 1920.*

Replying telegram 20th: This district has been all par practically since its inauguration of check-collection system. No collection by messenger or demands for payment in currency have been made by us except for a few days in one or two instances where nonmember banks failed to keep their promises to remit promptly. These cases were dealt with by forwarding checks for collection through express companies solely for the purpose of protecting Federal reserve bank against loss and ordinary methods of sending direct for remittances were readopted on receipt of satisfactory assurances that future remittances would be made promptly. It has never been practice of this bank nor, to my knowledge, practice of larger banks in this district to accumulate checks more than a day before forwarding for collection.

MORSS,
Governor Federal Reserve Bank of Boston.

NEW YORK, *January 22, 1920.*

Replying your telegram of 20th: First, this bank has never resorted to any method of coercion to compel State banks to join the Federal reserve system. Second, this bank has never attempted by threat or any coercive measure to require State banks to submit to any rule or regulation made by the Federal Reserve Board or any Federal reserve bank. Third, it has never been the policy of this bank to hold back any checks on any banks in the district for any purpose whatsoever. The only occasions—perhaps not more than three or four—where this has been done were due to our inability to secure the presentation of the items by agents or express company, as, for, example, during the strike of express company employees about one year ago. Fourth, it has been the practice of collecting banks in this district when they collect on non-member banks by sending items direct to hold back small items until they secure round amounts and thus avoid paying the maximum charge, but, as above stated, such practice has never been adopted or used by this bank. Fifth, the primary purpose of our use of express companies and private agents was, and is, to furnish a complete par-check collection system in this district for the use of our member banks, other Federal reserve banks, and through them for their member banks. This was the only method open to us to collect the checks drawn upon certain State banks and private bankers who had declined to remit at par for checks drawn upon them after the matter had been unsuccessfully taken up with these banks by letter, by personal visits, and by invitations to visit our bank. The appointment by us of agents for the collection of checks upon nonremitting State institutions was caused by their stamping their checks, "Not collectible through an express company," so that we had no other method of handling their checks. So far as we know and certainly not with our authority, have any threats, oral or written, been made by our agents. The total number of banks and bankers in this district upon which we are collecting checks is 1,702, of which but 4 State banks and 2 private bankers are being collected by express companies or agents.

CASE,
Federal Reserve Bank of New York.

PHILADELPHIA, PA., *January 21, 1920.*

Answering you telegram of yesterday, this bank has not used coercive methods and has deliberately refrained from any action savoring of a threat of any description either in securing membership in the Federal reserve system or in securing par collections throughout our district. Neither we, nor the larger banks in this district, have any occasion to hold back small items until they accumulate to some round amount. For a very brief period, not exceeding two weeks at most, we did use express companies, but we do not now use them nor any private agency in our collection service. Our policy has always been to invite application for membership from State institutions through excellence of our service and obvious advantages they may derive from such membership.

PASSMORE,
Governor Federal Reserve Bank of Philadelphia.

CLEVELAND, OHIO, *January 21, 1920.*

Answering your wire this bank has not used coercive methods to compel State banks to join Federal reserve system. All State banks on par list have been obtained by persuasive methods. No threats other than statement by our representative that we were obliged to collect their checks in justice to State banks which have voluntarily agreed to remit at par and that if they will not agree to do so we will collect through the express company or private agent. Checks on only two banks, both located in Kentucky, now being collected through express company, none through agents. Before par list was completed in this district a number of large collecting banks made a practice of holding small items until total amount was sufficient to avoid minimum charge and to save postage no longer necessary to hold items for that reason.

FANCHER.

RICHMOND, *January 21, 1920.*

Answering wire January 20: The Federal reserve bank of Richmond has never taken any step to coerce or compel a State bank to join the system or to require such bank to submit to rules or regulations made by Federal Reserve Board or this bank. Referring to matter of par collection of checks drawn on nonmember banks following methods have been followed in Maryland and to some extent in West Virginia. As the board knows, out of 29,586 banks in the United States, checks on all except 4,000 are collectible at par. The collection facilities of the Federal reserve system are open to all banks, whether members or nonmembers; to the member banks directly, to the nonmember banks through their member correspondents, and such facilities are being used to an ever increasing extent. In justice, therefore, to the 25,500 and odd member and nonmember banks whose names are on the par list we feel that it is our duty to attempt by all fair and reasonable methods to collect for them the checks on the remaining 4,000 banks, many, if not all of whom, are collecting on par points through members of the system. As the law does not allow us to pay the exchange upon the collection of checks it is incumbent upon us to devise some means of collecting without the payment of exchange to the bank on which the checks are drawn. Our procedure has been and is now to correspond with the nonpar nonmember banks explaining the situation. Failing to obtain results special representatives are sent to present the facts and argue to the justice of our endeavor with the officers of the banks. In the comparatively few cases in which neither of these methods was successful we arranged to present checks daily through a local agent selected by us; none, however, are acting at present. While it is in many places the custom of commercial banks to accumulate small items to avoid minimum exchange charges we have in no case accumulated items either for that purpose or for the purpose of embarrassing the bank by the presentation of checks amounting to an unusual sum at one time. On the contrary we have done everything in our power to avoid embarrassing situations and in the very few cases in which we have appointed agents we have instructed them to consult the convenience of the bank so far as it is practicable to do so, and under no circumstances to present checks in such a manner as to give rise in the community to any apprehension as to the standing of the bank or its ability to meet proper demands upon it in money.

SEAY.

ATLANTA, GA., *January 20, 1920.*

The Federal Reserve Bank of Atlanta has never received any instructions from the Federal Reserve Board nor has it with the consent or knowledge of the Federal Reserve Board resorted to any method of coercion to compel State banks to join the Federal reserve system, nor has the Federal Reserve Bank of Atlanta by threat or other coercive means attempted to require such State banks to submit to any rule or regulations made by the Federal Reserve Board or this bank. This bank has never held back checks on small banks until they amounted to considerable sums, and then sent messengers to make personal demand for payment in currency. This bank has not so far collected through duly appointed employees, and only in few instances has it collected through express companies. In the latter case there were no accumulations only those checks received in current day's work being sent forward to place of payment. It is the usual practice of large banks clearing out of town checks by sending direct to hold over for a day or so small checks until the aggregate reaches 100 or more, thus avoiding the payment of minimum charge of 10 or 15 cents which would be incurred on an item of small amount. The primary purpose of using express companies or paid employees to collect checks and drafts payable upon presentation drawn on banks that do not remit at par is to enable the Federal reserve banks to carry out

the provisions and intent of the Federal reserve act in so far as they relate to collection of checks and drafts payable upon presentation that are received on deposit from the sources named in the act. The act does not limit the checks that may be received on deposit to those drawn on member banks, and as it is clearly intended that we shall receive all checks and drafts payable upon presentation, and as section 13 interpreted by the Attorney General provides that no charges for remission shall be made against Federal reserve banks it of course follows that unless arrangements can be made with nonpar remitting banks to remit at par we must find a way of making collection that will not involve exchange charges. This bank has endeavored in every possible way to encourage nonmember banks to remit at par, and thus obviate the necessity of our arranging to present items for payment in cash and has from time to time offered to such nonmember banks the privilege of opening a clearing account for the purpose of collecting checks drawn on banks named in our par list, the balances so created to be used in remitting for items sent them by us, and any excess over the balance required against our average daily sendings to be subject to their order, we to inclose stamped envelope with each cash letter, and they to have the privilege of sending us in payment currency at our expense when more convenient. The privilege of opening a nonmember clearing account was offered so as to give them the benefit of our collection facilities if they desired to avail of them and not with the view of coercing them to become members of the Federal reserve system, for as a matter of fact many nonmember banks are not eligible from a standpoint of capital and requirement. There have been no threats, oral or written, by any one connected with this bank. We have stated to nonmember banks that while the Federal reserve act does not permit us to pay exchange for the remittance of bank checks and drafts payable upon presentation, we can incur any cost that is necessary in order to carry out the purposes of the act, and that we would very much regret to be forced to adopt other methods of collection that would prove embarrassing, annoying, and expensive.

ADELSON.

CHICAGO, *January 21, 1920.*

Replying to your wire, our policy in soliciting State bank membership is to point out its advantages and show where a State bank can be benefited by becoming a member. We certainly would not want any State bank to join the system unwillingly, or if it was not an advantage to it to do so. The same consideration is shown prospective State bank members as would be accorded them by a commercial bank soliciting their business. With regard to the collection at par of checks on nonmember banks, all such banks which were not on our par list January 1, 1919, have been visited by our representatives, who fully explained the advantages of the collection system, with a view to obtaining their friendly cooperation. When all banks in the States of Illinois, Indiana, and Iowa were placed on our par list there were a few which did not agree to remit for checks on them at par. (Checks on these banks were forwarded through the express companies for collection, a practice which is legitimate and which has been used in commercial banks for many years. In a few cases, where we were unable to obtain satisfactory service from the local express agent, and also at points where there was no express office, we held the checks a few days, and presented them by our messenger at the bank's counters for payment rather than have our messenger make daily trips. We are at present collecting through the express company checks on only one bank in Illinois, eight banks in Indiana, seven banks in Iowa, which have not agreed to par their checks, and are collecting checks on one town in Indiana and two towns in Iowa through agents which we have appointed. Our solicitors in obtaining par points have been instructed at all times to endeavor to obtain the good will and cooperation of the nonmember banks, and that coercive measures must not be used. We know of no cases where our agents or employees used any threats, oral or written.

McKAY.

ST. LOUIS, *January 22, 1920.*

Replying to your telegram to-day. This bank has never at any time coerced State banks into making application to join the system. On the contrary, we have made every effort to explain to banks making application both the advantages and disadvantages of membership. We have not wished to have any bank a member that did not thoroughly understand the workings of the system and appreciate the advantages. In collecting at par checks on nonmember banks there are only a few instances where we have found it necessary to make such collections by express or agent. The following excerpt from a letter addressed to the secretary of the Illinois Bankers' Asso-

ciation, under date of November 20, 1919, is indicative of our views and the policy pursued by us when it has been necessary to collect by express or agent: "One of our directors, Mr. Sam A. Ziegler, of Albion, Ill., mentioned to me yesterday a conversation he has had with you, from which he understood that it was your impression that it was the policy of this bank to hold up checks for several days, presenting same at one time, and demanding cash in all cases where it has been necessary for us to use other than the mails as a means of collecting checks. We are glad of this opportunity to advise you that such is not the case. We invariably see that the checks that we may through necessity have to present at the counter of a bank for payment in cash be presented promptly, the same as if they were transmitted through the mails. There have been some few instances where the action of the bank in returning items to us has resulted in more than one day's items reaching them at one time. This, however, has been unavoidable, and due entirely to the action of the bank on which the items are drawn, and not us." Several of the larger commercial banks in this district make it a habit to accumulate checks in order to avoid payment of minimum charges on small amounts. Purpose of collecting by express or agent is to avoid payment of exchange, and to obtain actual payment at par without assuming liability which would result if we were to authorize our agent or the express company to accept draft in lieu of currency. There has never been any occasion for our making any threats either oral or written in connection with our services in collecting at par checks on nonmember banks.

ATTEBERY, *Deputy Governor.*

MINNEAPOLIS, MINN., *January 21, 1920.*

Officers and employees of this bank have been cautioned repeatedly not to use any methods of coercion to compel State banks to join the Federal Reserve System. I have never heard this complaint from any State bank in this district, with the exception of one I called upon last summer that complained that they had been classed as unpatriotic because they had not joined the Federal Reserve System. I assured him that no such expression ever emanated from this bank, and upon further inquiry he intimated that the remark came from sources other than the Federal reserve bank or Federal Reserve System. As you know, we have conducted an active campaign for several years at a meeting to get State banks to remit at par with anything but satisfactory results. Early in December we wrote all nonpar banks in the States of Montana, North Dakota, and Michigan and told them we planned putting all banks in those States on our par list January 1, 1920, and it was optional with them whether we presented the checks at their counter for payment in cash or whether they preferred to remit without deductions for collection charges or exchange in funds immediately available. Some of the banks elected to remit, others told us we could present checks at their counter, and others refused to reply to our letter of inquiry, with the result that we made arrangements with the express companies and a few postmasters to collect checks for us on approximately 60 banks. This number has since been reduced to 43. We are now advising nonpar banks in South Dakota in the same manner, that all banks in that State will be placed on our par list February 1. As soon as facilities in our own bank warrant all banks in Minnesota and Wisconsin will be placed on a par basis. The officers and employees in charge of this campaign have been cautioned not to use any threats, but simply announce what we are going to do. I have just had them in my office, and they assure me no threats have been made by them. We have never held up a large amount of checks on any one particular bank, so that they would be embarrassed when cash was demanded. However, it has been our policy not to send one small check for collection on a nonremitting bank because of the expense, but we have waited until we accumulated at least \$100 in such checks. It has never been our intention to hold sufficient checks to be presented at one time so that the bank could not make payment in cash. Upon inquiry of the larger banks in Minneapolis I find that in the past they pursued a similar policy, but are not doing so at present. Our instructions to collecting express companies or private agencies are to present the checks and demand payment in cash, and if payment is not made, wire us immediately on items over \$500 regarding the items unpaid. Our par point campaign has been conducted almost entirely by correspondence. We have never employed any representative to solicit nonpar banks in this district. Glad to furnish copies of our circular letters and telegrams, if you feel they are necessary.

YOUNG.

KANSAS CITY, *January 21, 1920.*

Replying your telegram 20th: You are advised that—in so far as the Federal Reserve Bank of Kansas City, including its branches, is concerned—no method of coercion has been employed to compel State banks to join the Federal reserve system and no threats or other coercive means have been used or practiced to require such State banks to submit to rules or regulations made by the Federal Reserve Board or this bank. Under section 13, which prohibits Federal reserve banks from legally paying any fee to a member bank or nonmember bank for the collection and remittance of a check sent for collection, it has been necessary in certain cases to collect checks by such means as are available. In some cases there are no express companies and others where the express agents refuse for business reasons to handle collections. When such contingency arises and where we can not obtain a satisfactory local agent, it is necessary to send a messenger to present the checks at the counter of the payee. In cases where the payee bank is located in a distant town, for economic reasons we can not send messenger daily. About the only county in the tenth district where the banks have stubbornly resisted and treated with contempt our efforts to carry out the provisions of section 13 of the Federal reserve act as relate to collection of items at par is Pierce County, Nebr., all of the banks in which county are dominated to a greater or less degree by one Woods Cones, who has the moral support of C. A. McCloud, president of the First National Bank of York, Nebr., who is interested in several State banks also. The First National Bank of York for three years insisted upon charging this bank exchange on items sent to it and only desisted when advised by the comptroller that the publication of its statement showing as an asset action against the Federal reserve bank for exchange charges would be regarded as a misrepresentation of its condition. Until the development of the Federal reserve collection system it has been the practice of the city banks to hold small items against payee banks which charged exchange until such items amounted to at least \$100, in order to avoid prohibitory charges on small items of \$5 and \$10. It is not our practice to accumulate any specific amount or to hold checks over even for one day when sending them out for collection by mail or express; but where it is necessary to send a messenger—as in the case of Pierce, Nebr., 118 miles from our branch at Omaha—the cost of such visits warrants us in accumulating several days' checks for collection at once, assuming, of course, that any payee bank that preferred to pay checks on it over the counter in cash rather than to remit exchange at par for same would be always prepared to liquidate such demands in that way. Feeling sure that the complaints referred to in your telegram originated from Pierce, Nebr., we feel justified in going into some details regarding the collections of items of that town. The bankers of Pierce, by intimidation or otherwise, have prevented use of the facilities common to the public; as, for instance, the express agent not only refused to handle our collections but refused to accept a shipment of currency tendered to him by our messenger. This necessitates a visit to Pierce by automobile in order to carry to the next town funds that are paid. The notaries of Pierce were intimidated or influenced to the point where they were not available to our messenger when asked to protest items payment on which was refused. This required our messenger to take with him a notary from another town to legally present and protest items when refused for any reason. About a week ago Cones, McCloud, and others called a meeting of the State bankers at Omaha to discuss the Pierce campaign of the Federal reserve bank. At this meeting Cones, the principal speaker at the meeting, is reported to have made certain false and misleading statements.

MILLER.

DALLAS, *January 21, 1920.*

Answering your telegram date. The Federal Reserve Bank of Dallas has never through any of its officers or by any implied or direct sanction of the Federal Reserve Board, or its own board of directors, taken any steps toward or adopted any method of coercion to compel State banks to go into the system or has it by any threats implied or otherwise attempted to require nonmember State banks to submit to any rules or regulations made by the Federal Reserve Board or itself. The Federal Reserve Bank of Dallas in collecting checks on nonmember banks has never done otherwise than to recognize its right under the Federal reserve act and the regulations of the Federal Reserve Board to receive from its member banks, other Federal reserve banks and the Treasurer of the United States, negotiable checks and drafts drawn on any solvent bank, banker or trust company in its district, and to present and collect the face value of such checks through the most readily available channel. It has endeavored to avoid presenting checks either through express companies or its bonded agents for payment at face value in cash without first giving drawee banks the opportunity and

privilege of receiving checks on them by mail directly from the Federal reserve bank and remitting all face value on receipt for those checks good on their books in convenient exchange or currency or coin at expense of Federal reserve bank. Being fully cognizant of the fact that as shown by statistics, full 95 per cent of commercial transactions are settled by the medium of checks and drafts and considering at all times the business and financial interests of the entire eleventh Federal reserve district as reflected in the activities of both member and nonmember banks, it does not desire to withdraw cash from small localities in payment of checks except where necessary to collect fully face value of solvent checks which it receives. Its management fully realizes that such method of collection is wholly unnecessary unless made incumbent upon the Federal reserve bank by the refusal of drawee banks to pay without deduction checks drawn on them by their depositors when presented through other channels than at their counter. They also fully realize and appreciate that drawee banks can pay checks of their depositors presented them by making mail remittances drawn against the proceeds of checks which they have received on deposit themselves. The necessity for shipping currency to distant centers to pay such checks is minimized by reason of commercial settlements being made by the remittance of checks, and any expense of transportation of such small amounts of currency as may be necessary to cover the difference is absorbed by the Federal reserve bank. The Federal Reserve Bank of Dallas has never with any intent to embarrass a drawee bank permitted checks to accumulate in its possession from day to day, but has to some extent followed the established practice of commercial banks which handle collections in bulk to allow small checks to accumulate until they amount to as much as \$1,000 in order to reduce the percentage of cost of collection and handling to permit drawee banks to pay a number of small checks in one transaction. It may be well to inform you that in some instances, due to the refusal of drawee banks to pay the full face value of checks of their depositors to express agents or bonded agents when such checks were presented at the counters of the drawee banks and payment demanded and by reason of the express agents not following instructions and uniform rules established by the companies which they represent, occasionally a volume of checks has been thrown back on our hands which added to those in transit and those received by us on the date of receipt of such returned checks were subsequently presented by an agent of this bank as the holder of such checks and payment demanded and received. However, even in such few cases of this description where embarrassment to the bank was apparent our agent voluntarily accepted the bank's exchange in payment.

VAN ZANDT, *Governor.*

SAN FRANCISCO, *January 21, 1920.*

Federal Reserve Bank of San Francisco has not resorted to any method of coercion to compel State banks to join the Federal reserve system nor by any threats or other coercive means has the Federal Reserve Bank of San Francisco attempted to require State banks to submit to any rules or regulations made by the Federal Reserve Board. This bank does not hold back checks on small banks or any banks until they amount to a considerable sum then send them by any means to make demand for payment in currency to embarrass or coerce banks. Such action has not been taken by this bank. It is not the practice of large banks in this district when collecting on non-member nonpar banks to hold back small items until in round amounts they amount to \$100, except our Portland branch reports some banks in Portland hold items for no longer than two days. The only instance of what might be construed as coercive or threatening statements have been statements oral or written made by officers of this bank from time to time the types of which were that "the Federal reserve banks are by law not permitted to pay exchange and that if an exchange charge is made it will necessitate our collecting checks by whatever other means are available to insure their payment at par.

DAY.

