



FEDERAL RESERVE BANK  
OF DALLAS

Circular No. 2  
Series of 1924

February 25, 1924.

FINANCIAL STATEMENTS

**To the Member Bank Addressed:**

Regulation "A" of the Federal Reserve Board, Series 1923, provides in part as follows:

"A Federal Reserve Bank must be satisfied by reference to the note or otherwise that it is eligible for discount. The member bank shall certify in its application whether the note offered for discount has been discounted for a depositor other than a bank or for a non-depositor and, if discounted for a bank, whether for a member or a non-member bank. The member bank must also certify whether a financial statement of the borrower is on file with it.

"A recent financial statement of the borrower must be on file with the member bank in all cases, unless the note was discounted by a member bank for a depositor (other than a bank) or for another member bank, and—(unless)

"(1) It is secured by a warehouse, terminal, or other similar receipt covering goods in storage, by a valid prior lien on live stock which is being marketed or fattened for market, or by bonds or notes of the United States; or

"(2) The aggregate of obligations of the borrower discounted and offered for discount at the Federal Reserve Bank by the member bank is less than a sum equal to 10 per cent of the paid-in capital of the member bank and is less than \$5,000.

"A Federal Reserve Bank shall use its discretion in taking the steps necessary to satisfy itself as to eligibility. A Federal Reserve Bank may, in all cases, require the financial statement of the borrower to be filed with it."


While the foregoing regulation authorizes Federal Reserve banks to require financial statements in connection with all paper submitted for rediscount, heretofore the policy of this bank has been quite liberal in this respect, and it is not now intended to impose any unnecessary burden on member banks. However, after giving this matter its most careful thought, our Executive Committee has decided to request that in future copies of makers' recent financial statements be submitted in connection with all unsecured notes of \$1,000.00, or over, which may be offered to this bank for discount. Before taking this action the Committee gave due consideration to the inconvenience which sometimes attends the procuring of financial statements, but it was felt that the public is becoming so well educated in that connection that the difficulties formerly experienced have now been in large measure eliminated. It is believed, too, that the value of a financial statement is

much better appreciated by the banks now than was formerly the case. For these reasons, as well as others, it is thought that we are warranted in adopting the policy outlined above.

The Committee also feels that, regardless of whether or not offered to us for rediscount, it is manifestly to the interest of the member bank that an unsecured obligation of \$1,000 or over, particularly if acquired by a small or medium-sized bank, should be supported by the maker's statement showing his assets and liabilities in detail, submitted and considered prior to granting a loan. Such statement on file with the lending bank constitutes at once a protection to the officer making the loan, information to the directors supervising the bank's affairs and a guide to the bank examiner when conducting an examination.

In passing upon paper submitted to us for rediscount we are not unmindful of the value and protection which ordinarily the endorsement of a member bank affords to its customers' notes. However, our interpretation of the Federal Reserve Act and our conception of the function and responsibility of a bank holding the reserves of other banks compel the conclusion that the loanable funds of a Federal Reserve Bank should be invested only in that character of paper which carries with it such evidence of solvency and liquidity as will reasonably insure its payment, regardless of the endorsement of the member bank from which acquired. In no other way, in our judgment, can a bank of discount and issue properly discharge its duty to its depositors and the public generally. A policy of assembling the reserves of the district and then lending them back to the contributing banks, in varying amounts, merely against the responsibility of the borrowing banks' endorsement, would operate to deprive a Federal Reserve Bank of that independent strength and solvency necessary to safeguard the interests of all member banks. The vital importance of keeping a bank's reserve available at all times for its use in an emergency is well understood, and it therefore follows that when one of our members establishes and maintains its reserve with us as required by law it is entitled to feel that such reserve can be withdrawn and used in time of need, regardless of the condition or fortunes of other member banks. This statement is made for the purpose of assuring member banks to which notes may from time to time be returned that our action in that connection should not be construed as questioning the value of such endorsements.

Yours very truly,

A handwritten signature in cursive script, appearing to read "R. A. McKinney". The signature is written in black ink and is positioned centrally below the typed text "Yours very truly,".

Governor.