Rivell

4.

CONFERENCE BOARD OF GOVERNORS

FEDERAL RESERVE BANKS.

Evening Session, January 21, 1915.

WALTER. S. COX,
SHORTHAND REPORTER
COLUMBIAN BLDG. WASHINGTON, D.C.
PHONE MAIN 8324

CONFERENCE OF BOARD OF GOVERNORS, FEDERAL RESERVE BANKS.

EVENING SESSION.

New Willard Hotel.

Washington, D. C.,

January 21, 1915.

The Conference reconvened, pursuant to the taking of recess, at 9:30 o'clock p. m.

The Chairman: If Governor Wells will consent to act as Secretary pending the return of Mr. Curtis, we may now proceed with the business of the conference.

Before we adjourned we were considering the forms which had been submitted for a weekly report by member banks of the reserve condition and certain other items in their balance sheet. You will recall that we had taken the following action: We had recommended that the stated condition of member banks be confined to a statement of actual condition except as to the reserves, and that the reserves in the case of banks in reserve cities be calculated on the basis of both actual and average condition of reserves, and that all other items be the actual condition; and that the reports from country banks be of their actual condition as to all items, including reserves; that the brief form of report submitted for member banks in reserve cities be generally approved, and that the form of reports to be required of banks outside of reserve cities be reduced to not

greater length than that required of banks in reserve cities, and that the requirement for the calculation of reserve on the back of the statement be omitted so that the reserves stated be simply the amount in dollars and the percentage. The only item which we have not discussed and acted on in connection with this matter was the frequency of the report to be required of member banks, and I suggest that we now take up the question of the number of reports to be required from the member banks.

(The Secretary entered)

Mr. McCord: In order that the matter may be presented before the Conference I make the motion that the reports from the reserve cities be requested weekly and that the reports from the country banks be requested monthly.

The Chairman: You have heard Governor McCord's motion. Was that a second?

Mr. Mains: I second it.

The Chairman: Is there any discussion of Governor McCord's motion?

Mr. Aiken: Mr. Chairman---

The Chairman: I recognize Governor Aiken.

Mr. Aiken: In our district, Mr. Chairman, clearing house banks in reserve cities make a weekly statement which gives reasonably valuable information as to their condition. I cannot see any reason for imposing upon them the obligation to make a statement to the Federal Reserve Banks.

Mr. McCord: May I reply to that?

The Chairman: Certainly, sir.

Mr. McCord: They make it on Thursday or Friday?

Mr. Aiken: I do not care what day they make it. It makes no difference whether it is Monday, Tuesday or Wednesday.

Mr. McCord: The object of the department is, I think, to get an idea of the general condition of the country at certain intervals, and that information coming from the reserve city banks, would give them the barometer that they would naturally seek, and the others, coming monthly, would meet the full requirements, it seems to me.

Mr. Mains: I think so.

Mr. Aiken: As to that, Mr. Chairman, it seems to me that it makes no difference whether in one reserve city it is on Wednesday and in another reserve city it is on Thursday. I don't believe the day of the week, taking the country over, makes any difference.

The Chairman: Is it not a fact, gentlemen, that in these cities where there are clearing houses which it would include all the reserve cities, that the reports of the condition of the banks members of the clearing houses uniformly are required as of Friday?

Mr. Fancher: Ours is Thursday.

Mr. Wold: I do not think that is general. It is not in the Twin Cities.

Mr. C. Wells: We have reports in all reserve cities---

The Chairman: I am wrong, as usual.

Governor McCord, your motion has been seconded.

Mr. Seay: It occurs to me, Mr. Chairman, that if we would get monthly reports it would convey very little in-

formation as to the condition of the country, really.

Mr. Kains: I think it would convey all the information that is necessary. The amount of the accounts of all reserve banks really comes to about seventy per cent. I know that is the case in our district, and that would give, as Governor McCord says, the barometer, and would be less burdensome on the small banker in the country who does not understand anything about these statements. It would not be any hardship. They have to give it once a month.

Mr. Seay: I do not want to prolong this discussion. I do not see much advantage in requiring all the reserve cities to report unless we go out into the country. For some time past it has been true that the country bankers have held all the surplus reserves of the country. If you take the Comptroller's reports right through for a year past you will find that the country banks hold the surplus reserves. I do not think that would convey very much that would be enlightening information as to the state of the country. I was not in favor of the other banks being called on more frequently, but I do not see any necessity of calling on the reserve banks weekly and on the others monthly. I think it ought to be uniform.

Mr. McCord: Is not this true: That we all look forward to the clearings as reported by Bradstreet weekly, and they are an indication of the country largely?

Mr. Aiken: You get those now.

Mr. Seay: Yes; this is not a clearingquestion.

Mr. Aiken: Bradstreet will not stop reporting the returns of the country just because we get reports from those banks.

Mr. McCord: I understand that; but I am simply using that as an illustration, that it does have a bearing on the conditions, and that is what the Department evidently wants.

Mr. Seay: I have given a great deal of attention to Comptroller's reports and reports of that nature, and I believe that that kind of information would not be of any use to me. I have always been a student of those things, and I know that partial information is always misleading.

Mr. Kains: The proportion of the reserve cities is from one to two and a half. The country banks have one and the others two and a half; so that if a barometer was required, the weekly statement of the reserve cities would supply that barometer. The others are relatively unimportant.

The Chairman: Your motion was seconded, and it is your privilege to ask for the question unless someone offers some more discussion.

Mr. McCord: I simply made the motion in order to bring it to some proper state for discussion.

The Chairman: There is, however, a motion which has been seconded, and which should be acted upon or amended or withdrawn.

Mr. McCord: If any gentleman prefers it withdrawn, I will do that cheerfully. (Laughter)

Mr. C. Wells: I submit, Mr. Chairman, that Governor

McCord, having been successful in obtaining a second, ought not to withdraw his motion so soon, because he has said frequently that he could not get a motion seconded. (Laughter)

The Chairman: I have given you all fair warning that the order of business is progress, and I know you will not blame me if I try to make as much progress with the program as possible.

Mr. Aiken: I offer an amendment to the pending motion, that statements of the member banks be required monthly, and the others ~~short~~ the same term.

The Chairman: The motion was that weekly reports be required from banks in reserve cities and monthly reports from country banks. That has been amended to require reports monthly from both city and country banks, and from all member banks. Is there any further discussion?

There seems to be none. I will put the motion on the amendment.

(The motion on the amendment was put and carried.)

The Chairman: You will now vote on the original motion as amended.

(The motion, as amended, having been duly seconded, was put and carried.)

The Chairman: We have now adopted a motion which is, in effect, to recommend that those reports be required monthly from member banks. Is there any discussion on the subject of reports from member banks?

There seems to be no further discussion on the subject.

We will take up Item No. 16. At the last meeting of

the Governors the question arose as to whether the Federal Reserve Banks should receive from other Federal Reserve Banks notes payable in their district for collection. Two or three Federal Reserve Banks reported that they had received from other Federal Reserve Banks items of that character and were in doubt as to how they should deal with them. I would like to report that that matter has been submitted to the Federal Reserve Board; that is, it was submitted, as agreed at the last conference.

The question as submitted was answered with an opinion of the counsel of the Board who held, as I recall, that the collection of notes by one Federal Reserve Bank for another might fairly be construed as one of thoseincidental powers that were provided for by section 4 of the statute, as I recall, which defines the powers of the Federal Reserve Banks. Under the opinion of Judge Elliott I understand that we are now free to send notes for collection to the other Federal Reserve Banks, and that we are also free to receive for other Federal Reserve Banks for collection. If there is any question or debate on the matter we had better take it up now.

Mr. Fancher: Would not that matter of collecting the notes have some bearing on your intra-transit operations?

The Chairman: It doubtless would, Governor Fancher. That is to say it would make a certain amount of exchange. The bank at New York has rather taken the view that we have got to collect the notes with the discount by some method or other. Situations might arise that would make it inadvisable to send those notes for collection to the member

bank for whom they were discounted. We now have a ruling which will enable us to send them to some other Federal Reserve Banks. Certainly there is not anything in this Act which would prevent us from using any reasonable means to collect a note that we had discounted, even sending it to an attorney for collection; and our ability to employ the facilities of the system, it seems to me, is very properly construed by Judge Elliott, as being one of the incidental powers.

Mr. Seay: Is it your general practice to return the notes to the member banks after they have been discounted?

The Chairman: Our practice has been to do that on a certain number of days in advance, in order to obviate difficulties arising; and that is one of the things that is a subject on the program that we want to discuss.

Mr. Kains: I remember discounting $100,000, I think, of the Union Oil Company, and sending the notes to you for collection as they were payable in New York, and your office objected to that. This opinion of Judge Elliott would supersede your instructions given at that time?

The Chairman: Governor Kains, that happened some little time ago, and since then we have both the opinion of counsel and further light of our own counsel, and we will receive those notes for collection.

Is there any further discussion of item 10 on the program? If not, we will take up item No. 9, which bears somewhat on item No. 10.

At the last meeting it was decided, you will recall, to recommend to each federal Reserve Bank that the opinion of

their counsel be obtained as to the legal effect of the provision of the Fed ral Reserve Act which required member banks to waive demand, notice and protest on all notes which they rediscounted with Federal Reserve banks.

If you will permit a suggestion, I think we will make progress if we adopt the policy of having allof these opinions of counsel submitted to the Secretary of this meeting, mailed or delivered now, and that those opinions of counsel be submitted to the Federal Reserve Board in support of the conclusion as arrived at at this meeting, and that we do not take the time to read them; each of the Governors undoubtedly being familiar with the situation in his own district, based on those opinions.

The question is really whether this meeting shall make any recommendation to the Federal Reserve Board in regard to a mandatory provision of the statute that this waiver of demand, protest and notice be made a part of their discount transaction.

Mr. Aiken: I believe, Mr. Secretary, we have sent ours.

The Secretary: I have a copy of yours.

Mr. McCord: Mine is rather long, on account of having six cities to deal with.

The Chairman: May I ask that each of the Governors make a separate statement in regard to this matter?

Mr. Wold: Minnesota, North and South Dakota, Wisconsin, work under a negotiable instrument law, and I do not think that adding a waiver of demand, notice and protest would affect negotiability. As to Michigan, I am unable

to say. I am under the impression that Montana works under the negotiable instrument law. I think all of our territory is under the negotiable instrument law.

Mr. McCord: That could be checked by Rand-McNally.

Mr. Wold: I would like to ask a hypothetical question at this time in reference to that matter. If we had a piece of paper, discount paper, in New York City, on which our member bank has waived notice, demand and protest, and they require endorsement as to who have not waived, are we going to send that out, protest or no protest?

The Chairman: Governor Wold, may I suggest that as this is essentially a legal matter that we ask counsellor Curtis to make a statement for the record of his views in regard to the possibilities of difficulty arising by reason of this provision in the statute, and it may be that our discussion of the matter will be brought to a conclusion very much more promptly by listening to what he has to say.

The Secretary: I have not investigated the law with respect to states where the negotiable instrument law is not in effect. In the states where it is in effect I believe that the waiver by a member bank would probably have the effect of holding that member bank, but releasing prior endorsers in case the Federal Reserve Bank was negligent in presenting a note for demand or protest. On the other hand, there is a possibility that a certain phrase in the negotiable instrument law of most states, which provides that a party to a note is discharged by the discharge of a prior endorser might be held by the courts to discharge a party who provide that

had waived the demand, notice and protest by a prior endorser who had not waived it was discharged by the negligence of the holder.

Mr. Weed, the counsel of the Boston bank, wrote an opinion on that in which he cited the opinion of the late James Barr Ames, who was Dean of the Harvard Law School and who was instrumental in getting this Act passed. He felt that the provision was a very serious drawback to the act, and urged that it be not put in on the ground that it might operate to have this effect of discharging an endorser who had waived his rights because a prior endorser who had not waived was discharged.

My own view is that the provision was meant to be subordinate to the waiver, but the natural effect of the waiver is to give up your rights and to have a notice, demand and protest, and that the section of the statute meant other forms of discharge than discharge on something that you had already waived--- if I make myself clear.

But there is that doubt which has been expressed by very high authority on negotiable instruments, and consequently I feel that it is a bad thing to have in this law and to have as a mandatory requirement that the banks either ought to adopt a practice of having that waiver appear on the face of the instrument where it binds all subsequent parties or have the statute amended and that provision repealed.

The Chairman: From the standpoint of a layman and after discussion with Mr. Curtis this matter appears to me somewhat in this way: We are requiring from our member ban

a waiver of demand, notice and protest by virtue of this statute, which may result in their right of recourse against a prior endorser being imperiled or lost; and if, as a result of our negligence or even, possibly, as a result of causesthat may be beyond our control, that a member bank loses the right of recovery from a prior endorser, he might then use that as a defense to his own liability as an endorser. That situation might arise byw hich some bank, not possibly a bank that was in active operation and one that was in liquidation, whose affairs were in the hands of a receiver, where the receiver of the bank might feel under a legal obligation to the creditors of the bank to dfend the bank against the liability that he did not think could be enforced under the statute. The same kind of a danger arises when one is dealing with any fiduciary, no matter what he might regard to be his moral obligations--but nevertheless it follows as a matter of duty to his trust that he must employ every means that the law affords to require payment of the debt.

These questions of endorsement are more likely to arise in those cases where member banks fail than they are in the case of a going bank, because any going bank would not risk the impairment of its creditors by interposing such a defense. But if a large bank should

fail, with a very large amount of paper under rediscount, and some shrewd counsel should suggest that having rediscounted a lot of bad paper, and having a defense to their endorsement, they might then interpose this in an effort to avoid an honest liability; but as a matter of duty to the creditors of the bank it seems to me that the Federal Reserve Bank would be in a very unfortunate position. That, in a general way, expresses the view we have in New York; that is, the officers of the bank, generally speaking, the directors of the bank, seem to feel that it is a very bad provision of the act and ought to be repealed, possibly.

Mr. Wold: One more question, Governor Strong:

Assuming that the protest must release the bank where they have waived protest, and there are prior endorsers, could the Federal Reserve Bank sending a note to another bank for collection instruct the collecting bank to protest the nonpayment in order to protect its member bank and not release the prior endorser? Can it collect the protest even from the bank, inasmuch as it has waived protest?

Mr. McDougal: Mr. Chairman, may I read the concluding paragraphs of an opinion of our attorney bearing on that question?

The Chairman: Please do.

Mr. McDougal: (Reading):

"I am decidedly of the opinion that it would be ill-advised, however, to recommend any change in the law which would permit you to rediscount bills for member banks under an endorsement which did not waive demand, notice and protest, and this especially in view of the business necessity of

sending the bill to the member bank for attention on maturity.

"Under the present rule you at all times have a right to look to the member bank for payment, and I can well conceive of many contingencies under which the member bank might be relieved of payment if you had resting upon you the responsibility of making demand, giving notice, and protesting in order to hold them liable. If the bill were so endorsed, that demand, notice and protest were necessary to hold the member bank, it would be a strong reason why you should make collection through some other agency -- a practice not quite practicable under your system as now developed. Indeed, in my judgment, if you were to discount bills without the waiver you would not find it practicable to send them to the member bank from which they were received for collection.

" All the present difficulties of holding the prior endorsers would remain and added thereto would be the care required to take proper steps to hold the member bank."

That was his opinion.

The Chairman: Governor McDougal, that opinion, as I understand it, does not take into account the theory that Mr. Curtis advances, that there might be an implied release of the liability of the endorser that waived, provided the Federal Reserve Bank failed to get the note placed for payment promptly.

The Secretary: I ought to add, if you please, that I do not think that the theory of the law is correct, but it is an open question, so far as I know. There has never been a decision as to the exact meaning of the subsequent

section in the negotiable instrument law which provides that the subsequent endorser is discharged on the discharge of the prior endorser where the subsequent endorser has waived. I do not believe that he is discharged, but there is an opportunity to litigate that question.

Mr. Aiken: We have deemed it only safe to protest any notes that are not paid, in spite of the waiver and in spite of the risk we take of having to stand for the protest fees. Our cashier has been instructed to neglect the waiver entirely.

The Chairman: Do you collect your notes direct, Governor Aiken?

Mr. Aiken: Yes.

The Chairman: You do not send them to the member bank?

Mr. Aiken: Oh, we do send them to the member bank. Our local notes in Boston we collect there, every day at our counter from the rediscounting bank in the country. That is sent to them for collection.

The Chairman: Then the provision, as to demand, notice and protest really does not affect you, inasmuch as you put the burden of protesting on the member bank who has waived?

Mr. Aiken: That is true.

Mr. Kains: Some of our member banks are very much stirred up about that matter, on the theory that we would collect at some place foreign to themselves.

The Chairman: The difficulty in New York seems to be that member banks who have rediscounted paper with us are naturally inclined to feel that being a new organization we

may not be as careful as might be in conducting the details of business, and they would not care to risk the right of recovery against prior endorsers by negligence. I think their disposition would be to only offer us for rediscount paper which bore no prior endorsements, if possible, and that is a tendency that should if possible be arrested; because what we want is endorsed paper. I was hopeful that this meeting might arrive at some conclusion that would avoid the possibility of that discrimination against the rediscount of paper which bore prior endorsements.

Mr. Keims: It would require an amendment to the law. I would like to see the law amended. We can take care of ourselves.

Mr. Aiken: I would like to see it amended too.

The Chairman: It looks as though we might get a second to a motion.

Mr. Keims: Do you mean, move that we recommend that the law be amended?

The Chairman: I do not see any reason why you should not.

Mr. Keims: I will move that. I will start it, anyway.

Mr. Fancher: I second the motion.

The Chairman: Your motion, Governor Keims, is that the law be amended to strike out the provision as to the waiver of demand, notice and protest?

Mr. Keims: Yes sir.

The Chairman: Governor Fancher has seconded that motion, and as I recall the discussion the only opinion ad-

verse to that suggestion which has been advanced was made by Governor McDougal, who is supported by an opinion of his counsel, Mr. Powell.

Governor McDougal, have you any suggestion in regard to the motion?

Mr. McDougal: I would not be inclined to support that motion.

Mr. C. Wells: I would be disposed, Mr. Chairman, to decline to support the motion.

Mr. McDougal: I would like to know more about the effect it would have upon the legal status of the five states in our District. In Texas the law makes a provision for entering suit during the first term of the Court following the failure to pay, and by doing so holding the endorser. So that in Texas where the larger volume of business would naturally fall, we could protect ourselves by such procedure. It is the common practice to employ the w iver of demand, notice and protest among commercial banks.

Mr. Seay: On the face of the note?

Mr. C. Wells: Upon the face of the note or upon the endorsement.

Mr. Seay: I would rather take my changes to have either the waiver of the note, or, if not, to have all the endorsers subject to the general law.

Mr. Kains: That is it.

Mr. Seay: (Continuing) Rather than to have a single endorser waive. It seems to me it is bound to complicate the question from any point of view, if the waiver

is on the face of the note all are bound. If a single endorser waives and others do not waive, it is bound to add a complication the exact results of which I cannot say. I therefore think it would be ~~----~~ more logical not to have the provision in the law. I wonder if it was put there by a lawyer or an one who was accustomed to protect themselves by putting in all kinds of things of that kind that had anything to do with it, or whether it was put in there by a competent lawyer. I think it would be safer to have it out of the law.

Mr. McCord: Are the waivers on the face of the notes binding on all endorsers?

The Secretary: They certainly are under the negotiable instrument law.

Mr. McCord: But where the negotiable instrument law is not in effect?

The Secretary: I think the same would be true.

Mr. McCord: The question has not been decided in some of the states in my district -- Alabama, for instance, and others.

Mr. Wold: It occurs to me, Mr. Chairman, that we are about as well off with this waiver as we would be without it. The only paper we are bound to look after now is paper that has prior endorsements. But where there are no prior endorsements the waiver would hold and avoid taking care of the protests upon probably 75 per cent of the paper we take--- fifty per cent, at least.

The Chairman: Might it not become 100 per cent, after the banks have become affected with the idea that there is

some risk in taking paper of that character for collection? There will only be infrequent questions of possibility of the losses of claims against the prior endorser only by rediscounting paper which has no endorser, and they will get the poorest paper in the portfolios of the banks.

Mr. Wold: Possibly that is true. This question has different bearings in different parts of the territory. In our territory, for instance, it is the common practice with corporations not to take personal endorsements, but simply a guaranty covering the paper which a bank holds, and the question was raised as to whether or not a piece of paper if offered for rediscount by a bank had a guaranty of the stockholders, the guaranty saved the paper, and we felt satisfied that it did.

The Chairman: Might not this matter be settled by adopting this suggestion, Governor Kains, that your motion be amended so as to recommend that the law be amended providing that the waiver of demand, notice and protest be required on all notes rediscounted by member banks which bore no prior endorsement?

Mr. Kains: Yes. That would be all right.

Mr. Aiken: If there is no mention of it made, you could have the waiver put on. Any bank could have a waiver put on under those circumstances.

The Chairman: If the Act itself makes no such requirement, it is natural to suppose that the member banks will contend for the adoption of the practice that is common in banking, by which they would not be required to waive demand, notice and protest, because it certainly is

not customary for banks to require their customers to waive demand, notice and protest on paper that they rediscount.

Mr. Seay: I believe it would be against public policy to waive. There is many an endorser who has a very wholesome regard for a protest. Still, we take other paper we accepted without any exceptions to the last endorser, and why should there be variation in the method of handling the paper we rediscount for a member bank from that which would affect all other paper if we were in the general banking business. It has always occurred to me that it might lead some bank into error. Those who were not well informed might think they were actually waiving prior endorsements.

The Chairman: May I suggest that these Federal Reserve banks, after all, are just banks; they are not the Government; they are not entitled to the kind of protection that the Government always seems to have, of not having any liability or responsibility itself.

If this provision happened to be in the statute, we would be handling discounted paper just as any bank does, and ~~what~~ Governor McDougal's opinion, which is rendered by a lawyer whom I know personally, and for whom I have great respect, is based upon the theory that the Federal Reserve banks have been given some exemption here, and if they asked for an amendment to the statute they would be giving up something. Personally I would be inclined to contend that they have been given something by the statute which is unsound and contrary to common banking practice, and that we will all be safer in relying upon the customs that we

are familiar with and asking that this unusual provision be stricken from the statute and we go back to the methods that we are all familiar with.

Mr. O. Wells: I think that is rather a common practice, to have a waiver in our notes.

Mr. Seay: They would not be affected.

Mr. McCord: That is the common practice, but always the case that involves you has not got that in it.

The Chairman: Governor Kains' motion has been seconded, and no amendment has been offered. Have ~~the~~ we discussed this matter to a point where we are ready to vote on the recommendation for an amendment to the statute, or will someone suggest an amendment?

Mr. McCord: I happendd to be out when the motion was made.

Mr. Kains: I just moved that we recommend an amendment to the law in regard to this waiver.

Mr. McCord: I am prepared to vote.

(Cries of "Question".)

(The motion was put and declared by the Chairman to be carried, with two dissenting votes, Mr. McDougal and Mr. O. Wells voting no.)

Mr. Weld: When that recommendation gets there I wish they would recommend to the Federal Board that when they endorse checks they would endorse them in the proper way. They come through without any guaranty on them. They should require a guaranty.

The Chairman: Governor Weld, before we take that up I want to call attention to the fact that this goes before

the Federal Board as a recommendation, which is the first one we have made that has not been unanimous. Possibly it might be well to ask some one of those gentlemen who voted in favor of the motion to suggest some motion by which we could make a unanimous recommendation.

Mr. O. Wells: Is it necessary to report the vote? I think the majority should govern; unless Governor McDougal or myself should see fit to present a minority report, I think it should go as it is.

Mr. McDougal: It seems to me that the vote should stand as it is. We cannot always be united on all these subjects that come up.

The Chairman: Are you satisfied to have that recommendation go before the Federal Reserve Board without any minority report?

Mr. McDougal: I am perfectly satisfied.

Mr. O. Wells: I shall not present a minority report, I assure you.

The Chairman: That answers the only question in my mind.

Mr. Seay: It is a question not of mere banking practice, but a little at variance from the subjects we have brought to their attention before.

Mr. O. Wells: I think it is a question, in my own case, of not having advice of counsel sufficient to warrant an affirmative vote; and Mr. McDougal's counsel rather precluded an affirmative vote on his part.

The Chairman: If no objection is made the record will

be allowed to stand as it is, with the vote in favor of Governor Kains' motion.

Governor Wold, do you desire to bring up for the purposes of the record a suggestion with ~~Mm~~ regard to the method of endorsing checks which we remit to the Federal Reserve Board in payment of our expenses, and so on?

Mr. Wold: Yes. They have endorsed their checks for deposit only. We are unable to get a guaranty, and unable to get the Federal Reserve Board to change their methods. We have written them about it and asked them not to qualify their endorsement; but they say it is for protection.

(Informal discussion followed, which the stenographer was directed not to report; after which the following occurred:)

The Chairman: Governor ~~McKinzie~~ Wells, do you wish to bring this up for discussion now?

Mr. O. Wells: I am perfectly willing to bring it up now, or to defer it if you wish to go ahead with the program. It is only suggested to my mind because we have just made a recommendation for an amendment to the law, and I have it on my calendar to discuss, because we will get it some time or another, when it will be very desirable.

The Chairman: If it is the wish of the meeting we will take that matter up ~~with~~ as the next subject.

Mr. O. Wells: I will suggest, then, if there is no objection, that we take it up as the next subject.

Mr. McCord: The question before the House is that suggestion of Governor Wells', is it not?

The Chairman: Yes. What are the suggestions in regard to Governor Wells' plan of recommending that the Reserve Banks be permitted to make loans secured by eligible paper?

Mr. McDougal: Have you any idea as to why that was not permitted in the Act, Mr. Chairman? That would be a great satisfaction to us, if we were permitted to handle paper in that way.

Mr. O. Wells: I have an idea that it was left out of the Act because of the frequent discussions concerning the entire subject of commercial paper; and to leave it out of the Act will go far toward creating strictly commercial paper, or paper that is known as trade paper particularly.

Mr. McCord: Yes, that was the intention.

The Chairman: My impression is that the gentlemen who framed this bill believed the paper which was discounted by Federal Reserve Banks should be paid at maturity, and that if the banks dealt directly in making loans to member banks that it might necessarily establish a new class of paper where the loan would not necessarily be paid when it matured. You are dealing directly, then, with the original and only borrower, whereas, when you discount paper that has previously been discounted by a member bank, there is a third party who is obligated to pay the notes, and naturally there is no direct client of the bank who can come to you and ask for an extension. I believe, myself, that that was the real reason why collateral loans directly to member banks were not permitted in this act.

Mr. Wold: In view of the fact, Governor Strong, that the Board has intimated that there was no particular objection to our taking excess paper, holding it as security or collateral for those notes we did discount in those cases where it is necessary, that helps us.

Mr. McDougal: I have heard of such an intimation on the part of the Board, but I have seen the objection offered on the part of the discounting bank on two or three occasions. We declined to do it.

Mr. O. Wells: We can remain assured that unless we have an amendment to the law providing for the taking of collateral, that the obtaining of additional collateral would be very negligible. You would get very little of it.

Mr. Seay: You can decline to discount.

Mr. O. Wells: Yes; but that is discriminating against the applying bank and against the practice which you are following.

Mr. Seay: On just grounds, I believe.

Mr. Wold: I do not agree with you. There is no discrimination; if the two banks offer the same class of paper you would not discriminate.

Mr. Seay: You are discriminating against the class of paper they offer.

Mr. Wold: Because the paper is not standard paper. It is not such as you would care to accept.

Mr. Seay: I believe that while that would serve the convenience of banks it would be subversive of one of the vital principles of the Act. It is surely the purpose to

create in this country a class of paper of which there is not at this time a great abundance. I think we all appreciate the fact that if we did accept the direct obligations of the bank it would tend to make us lose a great deal of the the paper offered. Moreover it would not pay its loan; it would come to you for partial renewal, which is not the object of the act by any means. I believe it very wholesome, sir, that it should be that way.

Mr. O. Wells: Mr. Chairman, by way of expression, what do you think of that?

The Chairman: The desirability of making loans to member banks on commercial paper has never appealed to me. On the other hand, I am very strongly in favor of the reserve banks being permitted to make loans under certain conditions, secured by bank acceptances. There is a very strong, logical reason for thinking that, because there will develop in the course of time either certain banks or certain dealers who will accumulate large portfolios of acceptances, and unless the Reserve Banks are able to make loans on acceptances, that is, foreign bills that represent sales of commodities abroad or purchase of commodities abroad, it will be difficult to get the same freedom of dealing in bills in the market that prevails in every discount market we know anything of.

The practice in London, as you know, is to make so-called seven day loans. That is to say, the dealers in acceptances in the London market are able to negotiate a loan of seven days, and that is the way they carry their stock

of bills; and unless we develop such facility in the Federal Reserve Banks I can see that those seven day loans--- that is, the practicoof carrying those acceptances for dealers--- will naturally be cultivated by large reserve city banks. That, to my mind, is not a good development. Those banks would then be obliged to call their loans or buy the paper under pressure before they in turn could bring the paper to the Reserve Banks for rediscount, or for sale, if you please. They cannot take paper which they hold as collateral and go to the reserve bank and get it rediscounted without making some new bargain with the pledger of that collateral.

Mr. O. Wells: They cannot do that now.

The Chairman: They cannot do it now. As I say, Governor Wells, the desirability of the thing would be to let down the bars to the extent that the reserve banks be permitted to make the loans secured particularly by bank acceptances which they are authorized to discount or purchase under Section 14 of the Act. That, I think, would be a desirable amendment to the Act.

Mr. Kains: You mean, make loans at the face value of those acceptances?

The Chairman: Not necessarily, Governor Kains. As you know, the discount houses in London---

Mr. Kains: They take very slight advances. They lend 100,000 pounds on 101,000 pounds of paper, or less.

The Chairman: Exactly. That paper, at least those loans, are actually paid by the Bank of England, and the Bank of England does not even take the note from the borrow-

or, as a rule. They have a letter in their files which is somewhat similar to the general liability agreement that the banks have taken in the past from several exchange houses which simply gives the bank a claim of a certain character against the securities left as collateral to an advance, and I would like to see the reserve banks make the same class of loans secured by acceptances, but I am not yet convinced that it would be desirable to see the reserve banks able to make loans secured by commercial paper to member banks.

Mr. O. Wells: Even if it were restricted to eligible paper as collateral?

The Chairman: No; I do not think so. Frankly, Governor Wells, I did think so at one time, but I am rather inclined to feel the other way.

Mr. McCord: Mr. Chairman, does the Bank of England take a note at all with those collaterals attached? Do they not simply handle them on a guaranty agreement?

The Chairman: They do not take the note at all.

Mr. McCord: Is not that for the same reason, that they have a similar provision of law to what we have?

The Chairman: I do not think it is for the same reason. I do not think there is any restriction in the charter of the Bank of England that makes it necessary for them to do that. My recollection is that the Bank of England has practically no limitations.

Mr. Kains: No.

The Chairman: It has no dealings in that way with the market, but it is governed by years of precedent and prac-

tice that they regard as being just as sacred as law.

Mr. Kains: Some of them are the best firms in the world. There might be $100,000 from Hong Kong or Shanghai or India, and they take for them security in Arabia, and all over every gosh place, and they bundle them all together and do not even register them; put them in a bundle and take them over to a discount house. 250 pounds, sometimes, is all the margin there is on $150,000.

Mr. Seay: It is a general practice that has grown up from time immemorial, like the English constitution.

The Chairman: That is my impression, but I cannot say definitely that that is so.

Mr. Kains: I am sure that is so.

The Chairman: Governor Wells, we have discussed this matter at some length. Do you feel that this subject, No. 9 1-2 on my program, is a proper one now to take up by resolution?

Mr. O. Wells: I simply wanted an expression. If the Governors generally do not approve of the recommendation I am hardly prepared to urge it.

Mr. McCord: One of the members of the Federal Reserve Board----

Mr. Seay: I believe, Mr. Chairman, there is not a single thing that could be done that would so much tend to create the class of paper that we desire made in this country as that one movement.

Mr. O. Wells: What does the gentleman from Chicago think about that?

Mr. McDougal: I think we should not undertake to have that privilege granted.

Mr. O. Wells: What does the conservative City of Philadelphia say?

Mr. Rhoades: I do not favor loans based on commercial paper, as a rule.

Mr. O. Wells: How about Cleveland?

Mr. Fancher: The gentlemen may recall that in the discussion of rates and conditions before the Federal Reserve Board at our last meeting I brought to the attention of the Board a condition existing in our state. At that time by reason of the cattle embargo that really brought about a condition where a good many of our small banks were forced by that extraordinary situation to borrow money. They did not have in their portfolios short time paper. The probabilities were that embargo might last ten days or might last twenty days--- fifteen, twenty or twenty-five days--- and those banks needed that temporary assistance and did not have the short time paper to discount. Consequently we could not help them out. If it had been possible under conditions of that sort to have taken the bank's twenty day note we could have stepped into that situation and helped very materially. As it was they were forced by the Reserve Banks.

The Chairman: The corresponding banks?

Mr. Fancher: Yes; the reserve city banks.

Mr. O. Wells: There is not a day in the Federal Reserve Bank of Dallas where we are not given some material evidence of our ability to render a service to the member bank that

is not permitted to do this thing that has been suggested. We are an agricultural country where obligations are taken over longer periods than generally obtain in commercial sections of the country, and it would serve to put us on a parity with the customs prevailing among member banks of obtaining funds from their correspondents, and I apprehend that much of the prejudice against rediscounting comes through the unwillingness to change their methods of handling their bills payable. There is very little rediscounting in the eleventh district. There has been a great deal of hypothecation of paper securing bills payable, and it would enable us very readily to popularize the custom without relinquishing any of the principles involved in the eligibility of the paper or the principles involved in having an eligible paper. So far as the eleventh district is concerned, we would be doing no violence, in my opinion, to the excellent principles involved in the present practice, but we would be aiding an acceptance of the provisions of the Federal Reserve Act and rendering the Federal Reserve System more effective; but fearing that the hour has come when it would be difficult to obtain a second, perhaps, to a motion, I will not even offer a motion on No. 9 1-2. (Laughter)

The Chairman: Governor Wells has withdrawn from discussion No. 9 1-2, and unless there are some further remarks to be made, I will check that off as having been concluded.

Mr. Wold: I would like to add, Governor Strong, that in the ninth district it would enable us to extend credit

more broadly than is possible under the present method of rediscounting; but I do not think it is advisable to request the Federal Reserve Board to make an amendment of this kind at this time unless the system is so new that Congress might easily and reasonably say that we have not given it a fair trial yet. If, after a fair trial, you find it is necessary, then it will come to us and they will give you some relief. But we have not given it a fair trial yet. Until we do I do not think we ought to go to Congress and ask for any unnecessary amendments.

The Chairman: Gentlemen, we have put one item on the program that was developed from an inquiry which we made in New York prior to the last meeting of the Governors to throw a little light on the talk of shipping currency between the reserve banks. I asked Mr. Delanoy[illegible], of the firm of Delanoy[illegible] and Delanoy[illegible], who are very well known insurance brokers in New York, about the matter. Mr. Delanoy[illegible], by the way, is now in charge of the insurance bureau of the Government for marine insurance, the war risk bureau. I asked him to prepare a schedule of rates between all of the Federal Reserve Banks which will be based upon the very best practice that he could recommend by his office from their wide experience in that matter. As a result of that inquiry, he made arrangements for a syndicate of the largest underwriters of money shipments to submit quotations, and I have been informed that generally these quotations are below any that have heretofore been quoted for shipments of currency, although there may be some cases where they are slightly

above the expense of moving currency by other methods. Yet those who are acquainted with the matter tell me that they are the lowest rates that they have ever seen, generally.

Before coming to Washington Mr. Delaney called on me to say that he had arranged for this organization of insurers in order to be able to quote these low rates, and he was anxious that the Governors be informed of the fact that these arrangements had been made for their advantage, and he hoped if there were any considerable transactions, that these insurers who had really made an effort to quote very low rates, be given an opportunity to handle the business.

Mr. Kains: You mean, these firms mentioned here?

The Chairman: Yes. The statement has been furnished to each of the banks.

Mr. Wold: At this time?

The Chairman: No; at the last meeting. There is a typewritten sheet of paper, attached to the photographic schedules which give the names of insurers that have joined in making this offer. I explained to Mr. Delaney that almost all banks had for years been shipping currency, and had their own arrangements, which they did not like to disturb, but that I would submit this to the Governors, calling their attention to the fact that he had been good enough to get these rates, and suggest that if it afforded any economy in the shipments of currency which might be necessitated in settling balances between the reserve banks, consideration would be given to the effort that he has made to effect a real economy in settling these balances.

Mr. Kains: He has made some little error, in some way.

He has got the transit time from Chicago to San Francisco in one place given as five days, and San Francisco to Chicago as three days.

The Chairman: I think there was an error in one of those.

Mr. McCord: We have a better rate with a man in New York, about two and a half cents.

The Chairman: Than the one quoted there?

Mr. McCord: Yes.

The Chairman: It certainly goes without saying that the cheapest rate is what goes in these matters, and I feel that I have discharged my obligation in directing this matter to the attention of the Governors.

Mr. Rhoades: May I ask one question which is suggested by that? I understood that at the conference held here in October, it was suggested that all our surety bonds be with companies incorporated in the United States. We would like to get a blanket bond, such as Lloyd's write, for our force, and have refused to take it because of that recommendation, and I understand unofficially that some of the Reserve Banks had gone ahead and taken such blanket bonds, in spite of that recommendation. I would like to do that if the policy is not opposed to it.

The Chairman: We have blanket bonds at the bank in New York, but they are not written by a foreign company.

Mr. Fancher: So have we.

Mr. Keims: We have a blanket bond with the Royal Insurance Company.

Mr. Aiken: We have with the Massachusetts Bonding

Company.

Mr. McCord: We have a blanket bond with the United States Fidelity & Guaranty Company.

The Chairman: Is not Governor Rhoades' inquiry answered, then, by the statement that bonds can be obtained from American Companies?

Mr. Poncher: Is it a broad bond that covers most of the matters?

Mr. Aiken: I do not know whether it is or not.

(Informal discussion followed which the stenographer was directed not to report; after which the following occurred.)

The Chairman: Is there any further discussion on the bonding matter?

Mr. McCord: With reference to burglar insurance, I would like to know what rate we could obtain for burglary and daylight hold-up; or have you such bonds?

The Chairman: Governor McCord, I cannot answer the question as to rate. We can get that kind of insurance in New York, but I am unable to answer just now what we have in those matters.

Mr. O.Wells: We have burglar insurance, but the rate is about 97 1-2.

Rhoades:

Mr. Madden For three years?

Mr. Weld: The rate on burglar insurance could not necessarily be uniform. It all depends upon the character of the vault and the equipment you have.

The Chairman: And the location.

Mr. Wold: We have burglar insurance and daylight hold-up insurance, but what the rate is I cannot tell. There are different rates, because money is in different places at different times.

Mr. McCord: I have a rate of 65 cents for three years on a million dollars in burglary and daylight hold-ups. That is 21 5-12.

The Chairman: Gentlemen, I am afraid we are wandering into the details of bank management that might be disposed of at the bank without taking up our very valuable time.

Mr. Rhoades: I apologize, Mr. Chairman.

The Chairman: May I suggest that we now take up item No. 24 on the program, clearing house rules, concerning which the Federal Reserve Board would like to have some recommendation?

Mr. C. Wells: Just what does that include?

The Chairman: It was put on the program, Governor Wells, as a result of the ruling of the Federal Reserve Board made in response to an inquiry, I think, that came to New York, as to whether the Federal Reserve Bank in New York, ~~hxx~~ which had an immense amount of cash to handle in taking over the reserve transfers, might in fact establish rules with the clearing house of a limited character that would entitle it to receive as part of the reserve transfers the clearing house depository certificates that are due by the clearing house against the deposit of gold certificates and legal tenders and gold coin. That inquiry led to the Federal Reserve Bank of New York making application for a limited

membership in the clearing house which is somewhat similar to the membership that is enjoyed by the Treasurer of the United States at the Sub-treasury in New York. We are under no obligations of any kind to the clearing house except to pay a semi-annual fee for our privileges and except as to our liability in the event of any loss arising by reason of the shortage in the amount of money represented by the outstanding depository certificates, which is borne pro rata between the members of the clearing house. That is to say, if when an account of all the money held by the clearing house at the time the depository certificate is made it should be found that there is a shortage there--- and that, by the way, has never occurred--- why, then, all the banks of the clearing houses are pro rata liable for the loss. That liability we naturally do assume, particularly as we are now the owners and holders of, I think, more than one-half of all the depository certificates which are issued by the clearing house association.

The real question for discussion in connection with item No. 24 is whether the reserve banks should take membership of any kind in the clearing houses, or possibly, having done so, whether they should not report what the character of that relationship is, and whether any further recommendation should be made in regard to that matter, or any uniform policy adopted.

Mr. Keins: We joined the San Francisco clearing house, paying our full initiation fee, and while we would have liked to have joined in such manner as you did, under some such rule as the Assistant Treasurer, they would not take

us in in that way. One of our directors was president of the clearing house; another was the secretary of the clearing house committee. They would not take us in in that way. So I did not want to join that way, myself, but I allowed myself to be persuaded, and we have a certain liability in connection with the current gold. That is our vexed question out there. I do not mind taking my share with the rest of them, but I did not want to be a receiver for that stuff ultimately, so I am going to take measures to protect myself.

Mr. Wold: The Minneapolis bank has a limited membership in the Clearing House without any liability except to settle our clearings and get debit balances.

Mr. Seay: You are a bargain driver.

Mr. Aiken: I would like to ask if there is any Federal Reserve Bank that is not a member of the clearing house in the city in which it is located.

Mr. Fancher: We are not, in Cleveland.

Mr. McDougal: Speaking for Chicago, the Chicago Clearing House as a whole has taken formal action to invite the Federal Reserve Banks to join the Association, under the same terms that the Sub-Treasury enjoys. Our bank has not yet taken any action. We have had no need for the clearing house up to date, although if conditions should develop that we can use the clearing house, we will do so. Their action, I think, in the premises, was occasioned by the fact that our clearing house certificates such as Governor Strong has referred to as having been issued in New York, have been accepted by our bank in payment of the reserves.

Subsequently the banks which had paid these certificates in were informed by the clearing House that they had overstepped their authority on these certificates and they could not circulate outside of the membership. By inviting us in, or taking us in, as they may have done —— I believe they have done it—— that solves the question as to whether or not they are within their rights in paying their clearing house certificates to the banks depositing there, or paying a rent for reserve. We are not at present members of the clearing house.

The Chairman: As I understand it, all of the banks are members of the clearing houses except the one in Cleveland; and as to Chicago they probably are now, or if they are not they soon will be.

Mr. McDougal: That is a little strong, Mr. Chairman. We will be if the find that we need the Clearing House privilege.

Mr. Fancher: The situation in Cleveland is a matter that I took up with our clearing house association and it made it necessary for the constitution and by-laws to be amended to permit a membership such as Mr. McDougal speaks of. By following the requirements of cities having subtreasuries and where there are members of the Association, those amendments have been adopted, and the way has already been paved for our joining in a limited way by paying the annual charge of $200 for the privilege, and without having a vote or assuming a responsibility except the matter of shortage of accounts.

Mr. McCord: The Federal Reserve Bank of Atlanta has

joined the Atlanta Clearing House Association purely for the purpose of clearing, standing pro rata the expenses of the management; that is, the clerical cost and rent, and we are under no obligation; not subject to any of its rules and with no vote, but purely for the purpose of clearing.

The Chairman: We seem, in fact, to represent the Oligarchy of the Clearing House. I mean, we cannot lay claim to any exclusive privilege in that respect, and having been a little timid about suggesting what we ought to do in regard to Clearing House relations, I now feel quite free to join in the discussion of this matter, as we are all in the same boat.

The situation in New York is something like this: The New York Clearing House Association every day clears items aggregating from $250,000,000 to a maximum, I think, on the largest day, of over $700,000,000; and the clearings are handled at the clearing house by a staff of clerks now amounting to 130, about, that take the items to the clearing house. The only reason why it is possible to handle that volume today is that they really have two clearings through the clearing house. They have a preliminary clearing of large items, early in the morning, and a number of banks in New York, how many I cannot say, who have a night force of clerks, handle items that come in; that is, both city items and transit items and clearing house items, and in a recent conversation with a member of the clearing house committee who has been connected with banking for forty-eight years in New York, he told me that the best estimate he could make was

that every morning for about two hours twenty-five hundred men were engaged in New York banks making up clearing house reports. This information in regard to the volume of business going through the clearing house every day has been gathered together gradually by ~~xxxxxxxxxx~~ conversations, talking with those who are familiar with it, more familiar than I am, and I am convinced that today anything we that would disturb that situation which is being scientifically handled for the present would be an attempt to have a little bit of a stub tail wag a great big dog. The last thing that I want to see our bank undertake is the immense volume of business that might be thrown on us if any effort were made to unload that great transaction on the Federal Reserve Bank.

I do feel, however, that as the first step towards a more active participation in the handling of city checks the Federal Reserve Bank in New York can perform a really valuable service to the member banks if they settle their balances for them. There are twenty-nine members of the clearing house, exclusive of the Federal Reserve Banks, that are members of the Federal Reserve System.

If they made up two settling sheets every day it would mean that we would make either the paper due by all of the 29 member banks to settle with the state banks, or else we would receive the amount that was due to the 29 member banks and give them credit for it on our books and distribute it, and instead of handling 29 bundles of money in and out of the clearing house, when the balances are separated every day there would be only one. That is, instead of handling

30, including our own, there would only be one amount. The balances resulting from clearings of the New York Clearing House, running around nine, ten, twelve or fifteen millions, roughly, on a very active day, is an a very large amount. We have these balances running 50 or 60 millions. If three fourths of that represent the clearings and balances of the member banks and one fourth the state banks, which might not be out ofproportion at all, why, the reserve bank might have an active transaction every day in settling the balances of the member banks. It would have this very desirable result, I believe: It would be in effect a larger arrangement, or a credit arrangement, and would naturally lead to the member banks having a larger proportion of their optional reserve on deposit with the federal reserve bank, which I believe is a desirable thing to cultivate.

So that, speaking from the standpoint of the situation that is peculiar to New York, all that I hope to bring about in the near furture is an arrangement with the member banks by which we will settle their balances and go to the clearing house every day with their items, just as any other clearing house does.

Mr. Aiken: I do not know whether the gentlemen will be interested to know how that is worked with us in Boston. The second day or third day after we opened we began settling for all clearing house banks and did very well indeed. The banks like it, and it has increased the amount of money in the city very much, and it has been a very satisfactory arrangement.

Mr. Fancher: Have you kept your deposits against your clearing house certificates?

Mr. Aiken: There are no clearing house deposit certificates in Boston. When the Federal Reserve Bank was organized the clearing house storage certificates were all taken up and the money, most of it, was turned over to us, and we took all that the clearing house lent.

The Secretary: You have no trust companies in the clearing house?

Mr. Aiken: No; they are not members, but I do not think that makes any material difference. There is a small difference in the method of settlement.

The Chairman: The 36 state banks which I recall in the New York clearing house, and the 29 or 30 national banks, including federal reserve banks, would effect their clearings exactly as we have heretofore. The result of the clearings would not be one settling sheet showing all the debits and credits, but two; and the sum of the debits or credits, as the case might be, of the member banks would exactly equal the sum of the debits or credits, as the case might be, of the non-member banks, and one group would pay to the other, and we would simply pay the debits or receive the credits from the whole group of 29 or 30, including our own.

Mr. Aiken: We send our settling clerks and messengers to the clearing house just as any other bank does. The messenger of the clearing house has an account with us, and all the different banks pay him with a check on the

Federal Reserve Bank. He deposits this to his credit, and he pays the creditor banks with his check against this account. His debits offset his credits.

Mr. Wold: We have a peculiar situation in Minneapolis. The settlements must be made, of course, and ordinarily are made in gold, and in practice there is more or less jockeying. The rate of exchange is fixed by a committee of the clearing house every day, and the debtor bank, if New York exchange is at a discount, make that discount as small as possible. If it is at a premium the debtor bank urges that the premium be as large as possible, because the custom is not to settle in gold or to sell exchange and given the premium; or, if it is at a discount, have the discount as small as possible. For that reason they have not wanted to clear through the Federal Reserve Banks. They cannot settle this. They would have to cover in lawful money, and they do not care to do that.

Mr. Fancher: Are you a member of the Association?

Mr. Wold: Yes.

Mr. Fancher: How do they settle a debit with you? Do they pay you in lawful money?

Mr. Wold: We have charge account.

The Chairman: The entry on our program was a little bit blind in regard to clearing house relations, and all I had in mind was just such the kind of discussion we have had; but it seems to me that this very innocent little item attracted attention over in the Treasury Building, and they asked us to clear it up, with what object I do not know.

Might it not be well to take some action on that subject that would indicate what the sentiment of the Governors is in regard to the present relations with the clearing house?

Mr. O. Wells: Just for the purpose of having the record include a report from the various banks, I want to say that the Federal Reserve Bank of Dallas is holding membership by courtesy of the Clearing House Association, not being dignified by being in the position of the Sub-treasurer, but like the Post Office at Dallas, having a special membership without fee and without limit as to the length of time the privilege is extended. That privilege was granted with a view of opening clearing house arrangements as suggested by the Conference in October. You will perhaps remember what that was. I have an idea that the Board has put that down as one of the interesting numbers on the program because of the provision in the Act looking toward clearing house functions by the Federal Reserve Bord in various federal reserve cities, inasmuch as nothing has been done in that reppect.

The Chairman: Think of those five hundred millions of clearances in New York and those 2500 clerks we might have to employ if we got into this!

Mr. McDougal: Our membership comprises 21 banks of which five, I believe, are national banks, and members of the Federal Reserve Association. We are working out a plan now by which we hope to have balances settled at the Federal Reserve bank; a plan very similar to the one that has been described by you. We hope to bring that

about in time. It will be of great convenience to those banks and would at the same time relieve us, I think, of having a great deal of currency that is not only handled now at the clearing house, but handled before it goes there and after it gets back--- three times. We have a difficult problem there, more so than some of the other cities, owing to the fact that we have but few national banks in the clearing house.

The Chairman: Gentlemen, I really think we should make some definite report to the Federal Reserve Board on this item, and I should appreciate it very much if Governor McDougal would offer a resolution which would express his views, for the purpose of discussion, at any rate, of how this matter of clearing house relations should be developed.

Mr. McDougal: I do not believe I would be able to do that, Mr. Chairman.

Mr. McKay: There is a situation in Kansas City, Governor Strong, that I do not believe that anybody here has heard about ~~it~~, with regard to the clearing house. I had a letter from the manager of the Kansas City Bank in regard to the number to be assigned to the Federal Reserve Bank, and it was 18-4, and he said he was not going to use that number because it was possible that they might withdraw from the clearing house. It was on account of the amount of cash they were losing to the other banks, or some such reason as that, on account of taking in the whole district. So it is unfortunate that there is nobody here from Kansas City. I thought I would mention that, however, because they are

evidently having some trouble in Kansas City where they are a member of the Clearing House Association.

The Chairman: Mr. McKay, I think as you have mentioned Kansas City, I should state for the purposes of the record that I have received a telegram from Mr. Thrall in which he states that Governor Sawyer received word of the death of his mother just as he was about to take the train at Kansas City; that my telegram suggesting that some other representative of Kansas attend the conference had been received, but that Mr. Miller was at the present time in Texas, and that Mr. Sawyer and Mr. Miller absent it was impossible to have anyone here, with both

Mr. Fancher: I think that is quite unfortunate, in view of the transit discussion we will probably indulge in, that we have not someone from St. Louis or Kansas City to be with us.

Mr. Wold: I would like to ask Mr. McKay how they are going to settle these balances by virtue of the checks. They have got to give them something back, and it is just as easy to do it by the clearing house as it would be to clear them out over the counter.

Mr. McKay: They are going to have a decrease, of course, in the deposits, because they are charging them up and they have to pay them out to somebody----

The Chairman: Is it not just that way in which they are paying good money for the checks that they are buying in connection with this scheme of clearance?

Mr. McKay: Okay If they take on two or three million

dollars worth a day of transit items, they have to pay for them in cash, of course.

The Chairman: And in Kansas City they are members of the clearing house and the payment of these items is naturally settled through the clearing house, and their cash is tapped by that method, whereas otherwise it would be tapped by their direct transit payment.

Mr. Weld: If they were not members of the Clearing House, how would they settle balances? They would have to settle in some way.

Mr. McKay: They would ship currency, just as the country bank does.

Mr. O. Wells: But the member banks of the clearing house, Mr. Chairman, will withdraw, and if they have the necessary security, take it just as readily as they now take it.

The Chairman: That is just the same thing.

Mr. O. Wells: The point being that we did not understand Mr. Thrall's communication to Mr. McKay intimating their probable withdrawal from the clearing house as being any solution of the problem which they have before them.

~~The Chairman:~~ Mr. McKay I do not think it is, but he merely mentioned it. He did not say particularly why. I think it might have some bearing on this proposition.

~~Mr. McKay:~~ Mr. McCord Increase their difficulties. (Laughter) I will show you why. If they were not members of the clearing house, every bank would go there and draw money that they probably would not need, but after they were put into the clearing house they would settle on the difference.

Mr. O. Wells: Mr. Chairman, I move that we report to the Federal Reserve Board on item 24 that there seems to be no well defined policy or uniform policy of the various banks touching on the subject, and that therefore we have not at this time any report to make in reference to this subject.

The Chairman: Is that motion seconded?

(No response.)

Mr. Gold: I move it be the sense of this meeting that it is not advisable at this time even to consider the matter of clearing house functions other than settling the balances that may arise between the member banks.

The Chairman: Governor Gold has offered a resolution which may die, but which might be made a part of the record if somebody seconds it.

Mr. Keims: I will second Governor Gold's resolution.

(The motion, having been duly seconded, was put and carried.)

The Chairman: With an admonition in regard to the interjection of frequent motions and more infrequent seconds, I would suggest that we ask counsellor Curtis to report the status of the correspondence which we have had with the Federal Reserve Board in regard to the meaning of the term "lawful" money as it appears in various parts of the Federal Reserve Act.

The matter has not yet been disposed of, but as a report should be on our record, and may prove of value to the governors of the different banks, I think a very few

words from Mr. Curtis will enable us to complete the record as to item No. 29.

The Secretary: The correspondence arose from the fact that Mr. McKay, the Federal Reserve Agent, received one day $300,000 of silver certificates to reduce the liability of the bank for outstanding Federal Reserve notes, which had been received by the bank from him under the provisions of Section 16. After he had received it he was assailed with some doubts as to his right to receive that, and we consulted together as to whether or not it was within the meaning of that phrase in the law authorizing a bank to reducing its liabilities for outstanding notes by depositing with the Federal Reserve Agent gold, gold certificates, or lawful money, and whether he might receive silver certificates.

We drafted a letter to the Board asking for their ruling on that point. Mr. Jay received a reply from Mr. Willis to the effect that the Treasury Department has been accustomed to hold that lawful money meant legal tender money and that gold certificates and silver certificates were not properly legal tender or lawful money, but had been lawful reserve money for national banks by the act of 1882. And his communication ended at that point.

Mr. Jay and I thought it over with some care and decided that he had not quite answered the question. So we wrote again to him and said that we still had some doubts as to just what his reply meant, and asked him to place it before the Board for a formal ruling. We subsequently discovered that the first letter was Mr. Willis' own letter and not the

letter of the Board. It had not been before them. After some while we received a letter from the Board to the following effect, that while gold and silver certificates might not be lawful money, under a strict interpretation, it was the belief of the Board that they were intended to be included in the meaning of the phrase in Section 16, and that it was proper for federal reserve agents to receive silver certificates for the purpose of reducing the bank's liability. So that settled that particular inquiry.

Then we received a letter from the Treasurer of the United States saying that he was advised that we had outstanding ten million dollars worth of Federal Reserve Notes, and only $55,000 of redemption fund in gold, and requesting that we deposit $445,000 more in gold, redemption fund. To which we replied that the situation was that we had taken out ten million dollars worth of Federal Reserve notes, but that we had reduced our liability on all but $55,000 of the $10,000 by the deposit of gold, gold certificates or lawful money with the Federal Reserve Agent, and that to deposit $445,000 more of gold, ~~that~~ would make a total amount held against the exchange or redemption of the outstanding Federal Reserve notes on which our liability had not been reduced by such deposit to 104 per cent of the face of the notes. We sent a copy of that communication to the Board, but had no reply from the board or from the treasurer. I do not know what is coming on that.

Subsequently to that the Board of Directors of the Bank in New York requested an expression, if possible, from the

officers of the bank as to what they thought the phrase "lawful money" in the Federal Reserve Act meant; to which was made no reply. I have drafted a reply which I have here--- it is about five or six pages long--- in which I say that it seems to me that they do mean, in section 16 of this Act, to include as lawful money anything that is lawful reserve money, irrespective of whether it is legal tender or not, and that, secondly, the phrase in Section 16 does mean to include silver certificates and gold certificates in the places where gold certificates are not specifically mentioned in the section. That section mentioned them in two places, and does not mention them specifically in two other places, and I have adopted the view that it was immaterial whether they mention them or not; that they were really included in all places in Section 16. But I do not want to bind the Chairman by my view. He has read the letter, but has not passed any comment on it yet.

Mr. Adisman: Mr. Kains: May we have the letter in the record?

The Secretary: Yes, with pleasure. I have it here.

The Chairman: It is quite a long letter, and a very large part of it consists of references to and quotations from the Federal Reserve Act and the statutes, and I do not believe the reading of it now, Governor Kains, would ---

Mr. Kains: I just want it in the record so that we may digest those things.

The Chairman: It would be entirely agreeable to me. In fact, I would be very glad to have a copy of that taken into the record, if that is your desire.

The Secretary: I want to add for the purposes of this record that the letter has not yet been signed. It is in a rather formative state, but that is the conclusion I have reached. I have not forwarded the letter to Mr. Jay yet.

(NOTE: The letter above referred to will be found as an appendix to the record of the deliberations of the Conference.)

Mr. McCord: Mr. Curtis has raised the point which is probably collateral or subsidiary to the question he started out with, and I would like to know how he got around handing out that many notes without first putting the five per cent in the Treasury of the United States?

The Secretary: I am not as competent on that as the Chairman is.

Mr. McCord: By recent rulings, the chairman of our board will not issue to me Federal Reserve Notes until he actually has an acknowledgement from the Treasurer of the United States--not a sub-treasurer. I deposit it in the Sub-Treasury of New Orleans, and I have a statement from the Sub-Treasurer that he has received it, but under the recent ruling he has got to have it from the Treasurer in Washington.

Mr. Wold: My attention has been called to the fact that that wording of my resolution was just a little raw in one spot, and if it is in order I would like to have the words "even considered" stricken out.

The Chairman: Yes. By common consent, unless objection is made, Governor Wold will be permitted to withdraw the word "even".

The question raised by Mr. McCord, if I may be permitted to do so, I will have you consider as a separate subject and number it 30; and possibly you will permit me to start the discussion by stating what happened in New York.

We have in New York, towards the close of every year, a very active demand for clean currency. That is probably on account of Christmas day and Christmas shopping and the general demand for currency around the Christmas holidays. We had issued $1,000,000 of Federal Reserve notes and paid them out, or paid most of them out, and had deposited not $50,000 of gold in the redemption fund, but $55,000, just because we did not happen to have handy exactly $50,000 in bills of the right denomination without opening a safe to which access was quite inconvenient. So that the odd amount of $55,000 is of no significance.

When the demand for additional currency arose beyond the million dollars, the amount of our paper in portfolio had been so reduced by reason of its being paid that we were unable to get out any considerable additional amount of Federal Reserve notes. We reduced our liability on the notes which were outstanding by delivering gold certificates to the Federal Reserve Agent, and we took out of his hands an equal amount--- say a million dollars--- of the paper which we had recently pledged with him, which was of course specifically authorized by the act.

When the demand for additional currency was made on us, the Federal Reserve Agent was tendered a million dollars of paper which we had in the portfolio and thereupon he issued

to us another million dollars in Federal Reserve notes. And, again, when the demand arose, we reduced our liability by paying him another million dollars and taking out all notes that were in his hands, and again repledging them. That process was continued until we had, I think, in the neighborhood of six and a half millions of Federal Reserve notes. But by that time he only had $100,000 of bills that we could use for the purpose of taking out Federal Reserve notes. So the last transaction we had with him made it necessary for us to make thirty-four substitutions of the $100,000 in paper, in order to get out the last $3400,000 of Federal Reserve notes. (Laughter)

I do not hesitate to say that that occasioned some alarm in the minds of some members of the Federal Reserve Board. The transaction was completed and reported when Mr. Warburg and I were at White Sulphur Springs, and I had to face the music on returning to Washington on my way to New York.

The impression seems to exist in the minds of the Reserve Board that this was a method which would look up our gold reserves. As a matter of fact, it is a method by which we protect our gold reserve; and the matter was explained to them fully that we had not in any way violated the provisions of the Act, and I think now, individually, they are quite well satisfied that it was a perfectly proper thing to do.

On the other hand, there are three questions that have arisen in connection with it: One is whether or not the method of checking back the gold when we got back our Federal Reserve notes, without having to go through a redemption process in Washington, which of course would be a very

cumbersome thing to do; second, whether the Act does in fact require us to put up a five per cent redemption fund in gold with the Treasurer of the United States against the notes upon which, by the express provision of the Act we have discharged our liability by the deposit of gold or lawful money; and the third question is the one raised by the Federal Reserve Board, whether this process might not result in accumulating too much of our gold reserves behind notes issues which would remain in circulation for a considerable period of time.

The last question I do not think is really a question at all. It is a hypothetical possibility that would never arise. In the first place, as demands upon us for currency arise, we have got to meet them, either by issuing Federal Reserve notes, or by our reserves. If we pay out our reserves we reduce our gold. If we issue Federal Reserve notes, we retain our gold holdings as long as the notes remain in circulation.

Mr. O. Wells: That is, the Federal Reserve Agent retains them?

The Chairman: Yes.

Mr. McCord: The second point you raise is whether you are liable to five per cent?

The Chairman: As to the five per cent redemption fund, Governor McCord, that matter has just been dealt with in a long letter to the Treasurer of the United States of which a copy was sent to the Federal Reserve Board; and if the Governors desire, when we get a reply to that letter we

will have copies of it incorporated in the record.

Mr. Kains: I would very much like it. We have done the same thing to a moderate extent out in San Francisco.

Mr. McCord: I want to briefly call your attention to the wording of the law:

"but in no event less than five per cent."

The Secretary: "Not offset"--- is not that the next word--- "not offset by gold or lawful money"?

Mr. McDougal: If we should be fortunate enough to rediscount two million of paper, do you suppose you could prevail upon the reserve agent to let go of his gold?

The Chairman: I do not see how he could help himself, Governor McDougal, because that is what we would do then. We would ask him to issue to us two million of Federal Reserve notes against two millions of commercial paper, which he undoubtedly would do. There would be no reason for his not doing so. We would then have two millions of notes in our possession. We can at any time surrender notes in our possession to the federal reserve agents and get back gold which he holds, and the process would simply be reversed and we would have so much gold in our vault.

Mr. Seay: Unless that is a thoroughly legitimate proceeding I believe there is going to arise an occasion during the coming season for the issue of Federal Reserve notes against gold. Unless the large banks of the country do discount sufficient paper to enable them to issue Federal Reserve notes, the member banks will be called upon for currency, as usual, and the probability is that they will

have as usual to ship out their gold money, their lawful money. If, however, they could deposit their gold in the Federal Reserve Banks, and the Federal Reserve banks would absolutely issue their notes against the gold, I have never been able to understand why there was not a provision in the law for the issue of Federal Reserve Notes against gold, and them they could take new notes and issue gold against it, and the gold would be corralled in Federal Reserve Banks, and it would be a very fine opportunity to get it there. But it occurred to me that there should be an amendment to the Federal Reserve Act authorizing the banks to issue.

The Chairman: Governor Seay, would it be your judgment that we should submit a recommendation to the Federal Reserve Board in an alternative form, first, that it is the sense of this meeting that the Federal Reserve Act should be amended so that the Federal Reserve banks might issue Federal Reserve notes directly against an equal amount of gold or gold certificates; second, if it is impracticable for the Federal Reserve Board to take steps to secure such an amendment to the Act, that they consider and give necessary rulings that will justify the Federal Reserve Banks in following the procedure which I have described as having been followed in New York, so that the same result can be accomplished? That recommendation to the Federal Reserve Board I believe would be about the only thing now required to enable them to take a definite position in regard to the issue of Federal Reserve notes in those cases where there was not sufficient discounted paper in the hands of the

Reserve banks to arrange for it to issue by the pledge of the paper. Personally, I am very anxious to see that matter disposed of before the demand for currency arises.

Mr. Seay: It is, Mr. Chairman, and I have put that down as No. 30 upon the program to suggest to you at this meeting here. I think the matter is of such importance that it may well be suggested to the board in just the form in which you have stated it. You have expressed my mind as well as or better than I could have done it myself.

Mr. Weld: Has there been a ruling prohibiting that?

The Chairman: There has been no ruling prohibiting that, but I understand that a communication has been made to Mr. Jay: I have not been able, yet, to read it. It was either an opinion of counsel for the Federal Reserve Board, or, possibly, a ruling made to some other Federal Reserve Bank that Federal Reserve agents would not be authorized to make additional issues of federal reserve notes to the bank to which they were accredited so long as the Federal Reserve Banks had unissued Federal Reserve notes in their hands.

Mr. Weld: If they had none in their hands they might do it. I might say that we did the same thing in a modest way in Minneapolis. The Federal Reserve Agent agreed with me that it was a useless waste of energy to go through those amounts, and he said, "It looks good to me"; and I paid in gold for federal notes direct.

The Chairman: May the statement I made in the form of a suggestion be considered as a motion by Governor Seay?

Mr. Seay: Yes sir.

(The motion was numerously seconded, put and carried.)

Mr. Kains: I move we adjourn.

Mr. McDougal: I second the motion.

(An informal discussion here followed, which the stenographer was directed not to report; after which, at 12:12 o'clock a. m., the Conference adjourned until Friday, January 22, 1915, at 10 o'clock a. m.)
