332.3 - Fifteen Day Paper

TRANSFER

(F.R.) CONFIDENTIAL

(F.R.) CONFIDENTIAL

FEB 2 1953

My dear Mr. Martin:

Pursuant to provisions of Budget Circular A-19, and the delegation of authority from the President referred to therein, the Bureau of the Budget has received a communication regarding the following legislative proposal:

Draft of proposed amendment to make Federal Home Loan Bank obligations eligible for 15-day advances by Federal Reserve Banks to their members.

(Draft submitted by Housing and Home Finance Agency)

Before advising the submitting agency of the relationship of the proposal to the program of the President, the Director of the Bureau of the Budget would appreciate receiving an expression of your views with respect thereto.

It would be appreciated if your reply could be received by February 12, 1953.

If it is desired to confer on this matter, please communicate with Joseph E. Reeve, Bureau of the Budget, 17th and Pennsylvania Avenue, N.W., telephone Code 189, Branch 2125.

In addition to your agency, requests for views have been transmitted to the following agencies:

Treasury Department

Sincerely yours,

Honorable William McChesney Martin
Chairman, Board of Governors of the
Federal Reserve System
Washington 25, D. C.

Roger W. Jones
Assistant Director,
Legislative Reference

Attention: Mr. George B. Vest
1046 Federal Reserve Building
Washington 25, D. C.

Enclosure: Copy of draft

Orig filed 041.

FOR FILES
M. B. Treakle

SECTION 13 OF THE FEDERAL RESERVE ACT L-566

(U.S.C. refers to United States Code; CCH refers to Commerce Clearing House Bank Law Federal Service; P-H refers to Prentice-Hall Federal Bank Service.)

file date
APR 16 1938

1. Receipt of deposits and collections

Sec. 13. Any Federal reserve bank may receive from any of its member banks, and from the United States, deposits of current funds in lawful money, national-bank notes, Federal reserve notes, or checks, and drafts payable upon presentation, and also, for collection, maturing notes and bills; or, solely for purposes of exchange or of collection, may receive from other Federal reserve banks deposits of current funds in lawful money, national-bank notes, or checks upon other Federal reserve banks, and checks and drafts, payable upon presentation within its district, and maturing notes and bills payable within its district; or, solely for the purposes of exchange or of collection, may receive from any nonmember bank or trust company deposits of current funds in lawful money, national-bank notes, Federal reserve notes, checks and drafts payable upon presentation, or maturing notes and bills: Provided, Such nonmember bank or trust company maintains with the Federal reserve bank of its district a balance sufficient to offset the items in transit held for its account by the Federal reserve bank: Provided, further, That nothing in this or any other section of this act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, to be determined and regulated by the Board of Governors of the Federal Reserve System, but in no case to exceed 10 cents per $100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise; but no such charges shall be made against the Federal reserve banks. (U.S.C., title 12, sec. 342; CCH ¶¶215, 216, 217; P-H ¶4901)

2. Discount of commercial, agricultural, and industrial paper

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice and protest by such bank as to its own indorsement exclusively, any Federal reserve bank may discount notes, drafts, and bills of exchange arising out of actual commercial transactions; that is, notes, drafts, and bills of exchange issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used, or are to be used, for such purposes, the Board of Governors of the Federal Reserve System to have the right to determine or define the character of the paper thus eligible for discount, within the meaning of this Act. Nothing in this Act contained shall be construed to prohibit such notes, drafts, and bills of exchange, secured by staple agricultural products, or other goods, wares, or merchandise from being

eligible for such discount, and the notes, drafts, and bills of exchange of factors issued as such making advances exclusively to producers of staple agricultural products in their raw state shall be eligible for such discount; but such definition shall not include notes, drafts, or bills covering merely investments or issued or drawn for the purpose of carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States. Notes, drafts, and bills admitted to discount under the terms of this paragraph must have a maturity at the time of discount of not more than 90 days, exclusive of grace. (U.S.C., title 12, sec. 343; CCH ¶218; P-H ¶4908)

3. Discounts for individuals, partnerships, and corporations

In unusual and exigent circumstances, the Board of Governors of the Federal Reserve System, by the affirmative vote of not less than five members, may authorize any Federal reserve bank, during such periods as the said board may determine, at rates established in accordance with the provisions of section 14, subdivision (d), of this Act, to discount for any individual, partnership, or corporation, notes, drafts, and bills of exchange of the kinds and maturities made eligible for discount for member banks under other provisions of this Act when such notes, drafts, and bills of exchange are indorsed or otherwise secured to the satisfaction of the Federal reserve bank: Provided, That before discounting any such note, draft, or bill of exchange for an individual or a partnership or corporation the Federal reserve bank shall obtain evidence that such individual, partnership, or corporation is unable to secure adequate credit accommodations from other banking institutions. All such discounts for individuals, partnerships, or corporations shall be subject to such limitations, restrictions, and regulations as the Board of Governors of the Federal Reserve System may prescribe. (U.S.C., title 12, sec. 343; CCH ¶¶ 219, 220, 221; P-H ¶4908)

4. Discount or purchase of sight drafts

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice, and protest by such bank as to its own indorsement exclusively, and subject to regulations and limitations to be prescribed by the Board of Governors of the Federal Reserve System, any Federal reserve bank may discount or purchase bills of exchange payable at sight or on demand which grow out of the domestic shipment or the exportation of nonperishable, readily marketable agricultural and other staples and are secured by bills of lading or other shipping documents conveying or securing title to such staples: Provided, That all such bills of exchange shall be forwarded promptly for collection, and demand for payment shall be made with reasonable promptness after the arrival of such staples

at their destination: Provided further, That no such bill shall in any event be held by or for the account of a Federal reserve bank for a period in excess of ninety days. In discounting such bills Federal reserve banks may compute the interest to be deducted on the basis of the estimated life of each bill and adjust the discount after payment of such bills to conform to the actual life thereof. (U.S.C., title 12, sec. 344; CCH ¶¶ 222, 223, 224; P-H ¶4916)

5. Limitation on discount of paper of one borrower

The aggregate of notes, drafts, and bills upon which any person, copartnership, association, or corporation is liable as maker, acceptor, indorser, drawer, or guarantor, rediscounted for any member bank, shall at no time exceed the amount for which such person, copartnership, association, or corporation may lawfully become liable to a national banking association under the terms of section 5200 of the Revised Statutes, as amended: Provided, however, That nothing in this paragraph shall be construed to change the character or class of paper now eligible for rediscount by Federal reserve banks. (U.S.C., title 12, sec. 345; CCH ¶¶225, 226; P-H ¶4922)

6. Discount of acceptances

Any Federal reserve bank may discount acceptances of the kinds hereinafter described, which have a maturity at the time of discount of not more than 90 days' sight, exclusive of days of grace, and which are indorsed by at least one member bank: Provided, That such acceptances if drawn for an agricultural purpose and secured at the time of acceptance by warehouse receipts or other such documents conveying or securing title covering readily marketable staples may be discounted with a maturity at the time of discount of not more than six months' sight exclusive of days of grace. (U.S.C., title 12, sec. 346; CCH ¶¶227, 228; P-H ¶4927)

7. Acceptances by member banks

Any member bank may accept drafts or bills of exchange drawn upon it having not more than six months' sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. No member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, or corporation to an amount

equal at any time in the aggregate to more than ten per centum of its paid-up and unimpaired capital stock and surplus, unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance; and no bank shall accept such bills to an amount equal at any time in the aggregate to more than one-half of its paid-up and unimpaired capital stock and surplus: Provided, however, That the Board of Governors of the Federal Reserve System, under such general regulations as it may prescribe, which shall apply to all banks alike regardless of the amount of capital stock and surplus, may authorize any member bank to accept such bills to an amount not exceeding at any time in the aggregate one hundred per centum of its paid-up and unimpaired capital stock and surplus: Provided further, That the aggregate of acceptances growing out of domestic transactions shall in no event exceed fifty per centum of such capital stock and surplus. (U.S.C., title 12, sec. 372; CCH ¶¶ 229, 230, 231; P-H ¶4932)

8. Advances to member banks on promissory notes

Any Federal reserve bank may make advances for periods not exceeding fifteen days to its member banks on their promissory notes secured by the deposit or pledge of bonds, notes, certificates of indebtedness, or Treasury bills of the United States, or by the deposit or pledge of debentures or other such obligations of Federal intermediate credit banks which are eligible for purchase by Federal reserve banks under section 13(a) of this Act, or by the deposit or pledge of Federal Farm Mortgage Corporation bonds issued under the Federal Farm Mortgage Corporation Act, or by the deposit or pledge of bonds issued under the provisions of subsection (c) of section 4 of the Home Owners' Loan Act of 1933, as amended; and any Federal reserve bank may make advances for periods not exceeding ninety days to its member banks on their promissory notes secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act. All such advances shall be made at rates to be established by such Federal reserve banks, such rates to be subject to the review and determination of the Board of Governors of the Federal Reserve System. If any member bank to which any such advance has been made shall, during the life or continuance of such advance, and despite an official warning of the reserve bank of the district or of the Board of Governors of the Federal Reserve System to the contrary, increase its outstanding loans secured by collateral in the form of stocks, bonds, debentures, or other such obligations, or loans made to members of any organized stock exchange, investment house, or dealer in securities, upon any obligation, note, or bill, secured or unsecured, for the purpose of purchasing and/or carrying stocks, bonds, or other investment securities (except obligations of the United States) such advance

shall be deemed immediately due and payable, and such member bank shall be ineligible as a borrower at the reserve bank of the district under the provisions of this paragraph for such period as the Board of Governors of the Federal Reserve System shall determine: Provided, That no temporary carrying or clearance loans made solely for the purpose of facilitating the purchase or delivery of securities offered for public subscription shall be included in the loans referred to in this paragraph. (U.S.C., title 12, sec. 347; CCH ¶¶232, 233; P-H ¶4939)

9. Aggregate liabilities of national banks

Section fifty-two hundred and two of the Revised Statutes of the United States is hereby amended so as to read as follows: No national banking association shall at any time be indebted, or in any way liable, to an amount exceeding the amount of its capital stock at such time actually paid in and remaining undiminished by losses or otherwise, except on account of demands of the nature following:

First. Notes of circulation.

Second. Moneys deposited with or collected by the association.

Third. Bills of exchange or drafts drawn against money actually on deposit to the credit of the association, or due thereto.

Fourth. Liabilities to the stockholders of the association for dividends and reserve profits.

Fifth. Liabilities incurred under the provisions of the Federal Reserve Act.

Sixth. Liabilities incurred under the provisions of the Reconstruction Finance Corporation Act.

Seventh. Liabilities created by the indorsement of accepted bills of exchange payable abroad actually owned by the indorsing bank and discounted at home or abroad.

Eighth. Liabilities incurred under the provisions of section 202 of Title II of the Federal Farm Loan Act, approved July 17, 1916, as amended by the Agricultural Credits Act of 1923.

Ninth. Liabilities incurred on account of loans made with the express approval of the Comptroller of the Currency under paragraph (9) of Section 5200 of the Revised Statutes, as amended.

Tenth. Liabilities incurred under the provisions of section 13b of the Federal Reserve Act. (U.S.C., title 12, sec. 82; CCH ¶¶234, 5181; P-H ¶4945)

10. Regulation by Board of Governors of discounts, purchases and sales

The discount and rediscount and the purchase and sale by any Federal reserve bank of any bills receivable and of domestic and foreign bills of exchange, and of acceptances authorized by this Act, shall be subject to such restrictions, limitations, and regulations as may be imposed by the Board of Governors of the Federal Reserve System. (U.S.C., title 12, sec. 361; CCH ¶235; P-H ¶4951)

11. National banks as insurance agents or real estate loan brokers

That in addition to the powers now vested by law in national banking associations organized under the laws of the United States any such association located and doing business in any place the population of which does not exceed five thousand inhabitants, as shown by the last preceding decennial census, may, under such rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life, or other insurance company authorized by the authorities of the State in which said bank is located to do business in said State, by soliciting and selling insurance and collecting premiums on policies issued by such company; and may receive for services so rendered such fees or commissions as may be agreed upon between the said association and the insurance company for which it may act as agent; and may also act as the broker or agent for others in making or procuring loans on real estate located within one hundred miles of the place in which said bank may be located, receiving for such services a reasonable fee or commission: Provided, however, That no such bank shall in any case guarantee either the principal or interest of any such loans or assume or guarantee the payment of any premium on insurance policies issued through its agency by its principal: And provided further, That the bank shall not guarantee the truth of any statement made by an assured in filing his application for insurance. (U.S.C., title 12, sec. 92; CCH ¶¶236, 237, 238; P-H ¶4956)

12. Bankers' acceptances to create dollar exchange

Any member bank may accept drafts or bills of exchange drawn upon it having not more than three months' sight to run, exclusive of days of grace, drawn under regulations to be prescribed by the Board of Governors of the Federal Reserve System by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries, dependencies, or insular possessions. Such drafts or bills may be acquired by Federal reserve banks in such amounts and subject to such regulations, restrictions, and limitations as may be prescribed by the Board of Governors of the Federal Reserve System: Provided, however, That no member bank shall accept such drafts or bills of exchange referred to this paragraph for any one bank to an amount exceeding in the aggregate ten per centum of the paid-up and unimpaired capital and surplus of the accepting bank unless the draft or bill of exchange is accompanied by documents conveying or securing title or by some other adequate security: Provided further, That no member bank shall accept such drafts or bills in an amount exceeding at any time the aggregate of one-half of its paid-up and unimpaired capital and surplus. (U.S.C., title 12, sec. 373; CCH ¶¶239, 240, 241; P-H ¶4960)

13. Advances to individuals on direct obligations of United States

Subject to such limitations, restrictions and regulations as

the Board of Governors of the Federal Reserve System may prescribe, any Federal reserve bank may make advances to any individual, partnership or corporation on the promissory notes of such individual, partnership or corporation secured by direct obligations of the United States. Such advances shall be made for periods not exceeding 90 days and shall bear interest at rates fixed from time to time by the Federal reserve bank, subject to the review and determination of the Board of Governors of the Federal Reserve System. (U.S.C., title 12, sec. 347c; CCH ¶242; P-H ¶4964)

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

X-9636

FEDERAL RESERVE BOARD FILE

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 2, 1936.

Dear Sir:

You will find inclosed, for your information, a copy of a letter received by the Board under date of June 18, 1936, from the Administrator of the Federal Housing Administration, and a copy of the Board's reply of June 22, 1936, with respect to the question whether loans insured under the provisions of the National Housing Act are eligible as collateral for advances by Federal reserve banks to their member banks.

Very truly yours,

Chester Morrill

Chester Morrill,
Secretary.

Inclosures.

TO ALL PRESIDENTS.

COPY X-9636-a

FEDERAL HOUSING ADMINISTRATION
Washington

June 18, 1936

Honorable Marriner S. Eccles
Chairman, Board of Governors
Federal Reserve System
Washington, D. C.

Dear Mr. Eccles:

In the absence of any specific ruling by the Board of Governors of the Federal Reserve System, there appears to be a question in the minds of some member banks as to whether mortgage loans and modernization loans insured under the provisions of the National Housing Act are eligible as collateral for advances by the Federal Reserve banks.

My attention has been called to the fact, however, that one of the Federal Reserve member banks has recently asked the Federal Reserve Bank of its district "on what basis loans would be granted when secured by Federal Housing Administration mortgage or modernization loans," and has received from the Federal Reserve Bank the following answer:

> "Loans on the security of FHA Mortgage or Modernization loans are not considered in the same category as the direct obligations of the United States or the guaranteed obligations such as Home Owners Loan Corporation bonds, and for that reason would not be eligible as collateral to a member bank's fifteen day note at our regular rediscount rate.
>
> "There is no reason, however, why they would not be considered under Section 10b, in which Section Federal Reserve Banks are authorized to make loans to member banks on any sound assets owned by the member banks. The Board of Governors has not yet issued its new Regulation A, but this is our interpretation of the Act."

Explaining its reasons for having sought to learn the attitude of its reserve bank with respect to loans insured by the Federal Housing Administrator, the member bank writes to me as follows:

> "This bank is very much interested in having as much liquidity attached to FHA mortgage loans and modernization loans as possible. We are planning to acquire all loans under both titles we can find in our community as long as

we have available funds. We are very much interested, however, in knowing these mortgages and notes would be readily acceptable at the Federal Reserve Bank as security for loans should we find it necessary to borrow."

The bank then makes the following suggestions with regard to the answer which it received from the Reserve Bank:

"Wouldn't it be possible for you to take this matter up with the Federal Reserve Board at Washington and procure from them a ruling that would be applicable to all Federal Reserve Banks? It is my opinion if you could obtain such a ruling, every banking institution in the United States would feel inclined to invest a larger portion of their surplus funds in these securities."

I realize that when most banks, as at present, have available a large surplus of funds for investment, there is no occasion for their having to apply to the Federal Reserve banks for advances against loans insured by the Federal Housing Administration. Nevertheless, it would be helpful, I believe, if a formal ruling could be had from the Board of Governors as to whether the Federal Reserve Bank whose letter I have quoted has, in the opinion of the Board, correctly interpreted Section 10(b) of the Federal Reserve Act, as amended by the Banking Act of 1935, insofar as it may be construed to apply to loans insured under the provisions of the National Housing Act.

I shall appreciate your considering this matter with a view to obtaining a ruling on these questions if it is agreeable to the Board to make one at this time.

Very sincerely yours,

(Signed) Stewart McDonald

Stewart McDonald
Administrator

X-9636-b

June 22, 1936.

Dear Mr. McDonald:

Pursuant to your letter of June 18, 1936, regarding the status under Section 10(b) of the Federal Reserve Act of loans insured under the provisions of the National Housing Act, I have brought to the attention of the Board your request for an expression of the Board's views on the letter recently written by one of the Federal Reserve banks to a member bank which had inquired "on what basis loans would be granted when secured by Federal Housing Administration mortgage or modernization loans."

The Board notes that the answer of the Federal Reserve Bank which you have quoted is as follows:

> "Loans on the security of FHA Mortgage or Modernization Loans are not considered in the same category as the direct obligations of the United States or the guaranteed obligations such as Home Owners Loan Corporation bonds, and for that reason would not be eligible as collateral to a member bank's fifteen day note at our regular rediscount rate.
>
> "There is no reason, however, why they would not be considered under Section 10b, in which Section Federal Reserve Banks are authorized to make loans to member banks on any sound assets owned by the member banks. The Board of Governors has not yet issued its new Regulation A, but this is our interpretation of the Act."

Section 10(b) of the Federal Reserve Act as amended on August 23, 1935, reads as follows:

> "Any Federal Reserve bank, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, may make advances to any member bank on its time or demand notes having maturities of not more than four months and which are secured to the satisfaction of such Federal Reserve bank. Each such note shall bear interest at a rate not less than one-half of 1 per centum per annum higher than the highest discount rate in effect at such Federal Reserve bank on the date of such note."

Any advance under this section must be secured to the satisfaction of the Federal Reserve bank, but there is no other limitation on the character of security which may be used for such an advance. Accordingly, it is the opinion of the Board that a Federal Reserve bank is authorized to make advances to a member bank under section 10(b) of the Federal Reserve Act upon the security of modernization loans insured under Title I of the National Housing Act or mortgage loans insured under Title II of the National Housing Act if such security is satisfactory to the reserve bank.

Of course the question whether such loans would in particular cases constitute acceptable security must be determined by the Federal Reserve banks as and when requests for such advances are received from the member banks, but, if satisfactory, the Federal Reserve banks are at liberty to make advances to member banks upon any such security in accordance with the provisions of section 10(b) of the Federal Reserve Act.

With kind regards, I am

Sincerely yours,

(Signed) Marriner S. Eccles

M. S. Eccles
Chairman.

Honorable Stewart McDonald
Federal Housing Administrator
Washington, D. C.

Honorable Wright Patman,
House of Representatives,
Washington, D. C.

Dear Mr. Patman:

In reply to your letter of May 24, there is inclosed a statement showing the aggregate amount of promissory notes of member banks taken by the Federal reserve banks during the calendar year 1931 and during January, February, and March, 1932.

In addition, there are shown on the inclosed table the average month-end holdings of such notes by the Federal reserve banks during 1931 and their holdings on the last day of each of the first three months of 1932.

Very truly yours,

(Signed) Chester Morrill

Chester Morrill,
Secretary

Inclosure

VF/CM/fsf

VOLUME OF MEMBER BANK PROMISSORY NOTES TAKEN BY THE FEDERAL RESERVE BANKS DURING THE CALENDAR YEAR 1931, AND DURING JANUARY, FEBRUARY AND MARCH 1932

Year 1931	$13,415,472,762
January 1932	3,188,775,958
February 1932	3,209,786,633
March 1932	2,334,890,670

AVERAGE MONTH-END HOLDINGS BY THE FEDERAL RESERVE BANKS OF MEMBER BANK PROMISSORY NOTES DURING THE CALENDAR YEAR 1931, AND THE AMOUNTS OF SUCH NOTES HELD ON THE LAST DAY OF JANUARY, OF FEBRUARY AND OF MARCH 1932

Month-end average 1931	$206,804,163
January 31, 1932	652,327,194
February 29, 1932	595,337,549
March 31, 1932	442,487,360

WRIGHT PATMAN
FIRST DISTRICT
STATE OF TEXAS

WASHINGTON ADDRESS:
545 HOUSE OFFICE BUILDING

M. Smead

Congress of the United States
House of Representatives
Washington, D. C.

RUSSELL M. CHANEY
SECRETARY

LUCILLE SPAIN
ASSISTANT

COMMITTEE ASSIGNMENTS:
DISTRICT OF COLUMBIA
CIVIL SERVICE
ROADS
WORLD WAR VETERANS' LEGISLATION
CHAIRMAN SUBCOMMITTEE ON HOSPITALIZATION

3323

May 24, 1932

Federal Reserve Board
Treasury Building
Washington, D. C.

Dear Sirs:

Kindly let me know the total aggregate amount of advances made to member banks on their 15-day promissory notes during the year 1931, and also the total aggregate amount advanced to member banks on their 15-day promissory notes during January, 1932; February, 1932; March, 1932.

Yours truly,

WP:LS

Wright Patman

Form 148b

#1.2

TELEGRAM

FEDERAL RESERVE BOARD
WASHINGTON

~~332.3~~
332.3

March 18, 1932

Calkins, San Francisco

Wire 3/15/32

Combining information furnished by you with that furnished by other Federal reserve banks in response to uur wire of March 15, shows that we will need same information for any additional banks in your district which had average daily borrowings during first half of 1929 in excess of $3,815,000. Please advise whether you had any such banks and if so, how soon information can be furnished.

SMEAD

ELS/fjc

FILE COPY

2—9454 GPO

TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

332.3

RECEIVED AT WASHINGTON, D. C.

3/16/32

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Boston Mar 16 345pm

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Washn

Twill 1449 fifteenth.

Young

405pm

U.S. GOVERNMENT PRINTING OFFICE: 1928 2—11901

TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

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3/16/32

RECEIVED AT WASHINGTON, D. C.

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TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

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10am

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TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

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3/15/32

RECEIVED AT WASHINGTON, D. C.

33cs 8

Philadelphia 1218p Mar 15

Smead

Washn

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Norris

1219p

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TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

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3/15/32

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RECEIVED AT WASHINGTON, D. C.

Cleveland 107p mch 15

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3/15/32

Fancher

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U. S. GOVERNMENT PRINTING OFFICE: 1928 2—11901

TELEGRAM

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FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

3/15/32

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155gb 5

Chicago Mar 15 1109am

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Washn

Twill 1449 3/15/32

Mcdougal

1213p

U. S. GOVERNMENT PRINTING OFFICE: 1932 2—11902

TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

3323

3/15/32

RECEIVED AT WASHINGTON, D. C.

170gmr 12

Saint Louis 1127a Mar 15

Smead

Washington

Twill 1449 March 15 1932.

Martin

1238p

U. S. GOVERNMENT PRINTING OFFICE: 1928 2—11901

TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

3323

3/15/32

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Kansas City 1055a Mar 15 RECEIVED AT WASHINGTON, D. C.

Smead

Washn

Twill 1449 3/15/32

Hamilton

104p

U. S. GOVERNMENT PRINTING OFFICE: 1930 2—11901

TELEGRAM

3323

3/15/32

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

RECEIVED AT WASHINGTON, D. C.

178gmr5

Dallas 1145a Mar 15

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Washn

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McKinney

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U. S. GOVERNMENT PRINTING OFFICE: 1926 2—11901

TELEGRAM

FEDERAL RESERVE SYSTEM

(LEASED WIRE SERVICE)

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3/15/32

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RECEIVED AT WASHINGTON, D. C.

Sanfrancisco Mar 15 1014am

Board

Washn 1449

Odorous uncurled rotative.

Calkins

127p

U. S. GOVERNMENT PRINTING OFFICE: 1928 2—11901

Form 148

15 Dec collateral notes.

TELEGRAM

FEDERAL RESERVE BOARD

LEASED WIRE SERVICE

WASHINGTON

2—9454 GPO

332.3

March 15, 1932 332.3

Young - Boston	Black - Atlanta	Hamilton - Kansas City
Norris - Philadelphia	McDougal - Chicago	McKinney - Dallas
Fancher - Cleveland	Martin - St. Louis	Calkins - San Francisco
Seay - Richmond	Geery - Minneapolis	

TRANS. 1449. In order to answer request of Senator Glass please wire not later than Thursday following data for each of the 5 banks in your district with the largest average daily borrowings from the Federal reserve bank on member bank collateral notes during the first six months of nineteen twenty-nine.

1. Average daily amount of member bank collateral notes held under discount for each bank (divide by 181 days).

2. Total number of calendar days including Sundays and holidays each bank was borrowing on member bank collateral notes.

3. Number of periods of one or more days duration that each bank was borrowing without interruption on member bank collateral notes. This number of periods divided into number of days reported under item two will give average duration of uninterrupted borrowings on member bank collateral notes.

4. Same data for same banks for first half of nineteen thirty-one.

Please also mail statement showing for each of such banks their borrowings from Federal reserve bank on each day in first half of nineteen twenty-nine and nineteen thirty-one, (a) on member bank collateral notes secured by Government obligations (b) on member bank collateral notes secured by eligible paper and (c) on rediscounts.

In our tabulations numbers will be substituted for names of banks given in your report.

(Signed)

Dr. Goldenweiser

The attached memorandum by Mr. Vest re extending the maturity of promissory notes of member banks secured by eligible paper may be of interest to you and Dr. Burgess in connection with the revision of the Glass Bill.

2/17/32

Walter Gyatt

Feb. 17, 1932.

PROPOSED AMENDMENT TO THE FEDERAL RESERVE ACT WITH REGARD TO ADVANCES TO MEMBER BANKS ON THEIR PROMISSORY NOTES.

The Federal Reserve Board in its annual reports for the years 1927, 1928 and 1929, recommended to Congress the enactment of an amendment to Section 13 of the Federal Reserve Act increasing from 15 to 90 days the maximum maturity of advances which may be made by Federal Reserve banks to member banks on their promissory notes secured by paper which is eligible for rediscount by Federal reserve banks; and in its annual report for 1929, the Board also recommended an amendment to this section of the Federal Reserve Act which would make debentures of Federal Intermediate Credit Banks eligible as security for advances by Federal reserve banks to member banks on their promissory notes for periods not exceeding 15 days. In the following paragraphs there are set forth the reasons why such amendments to the Federal Reserve Act are believed both important and desirable.

Under the present law, Federal reserve banks may rediscount for member banks commercial or industrial paper with maturities up to 90 days and agricultural paper with maturities up to nine months, and may make direct advances to member banks on their promissory notes secured by commercial, industrial or agricultural paper for periods not exceeding 15

days. An amendment to the law, therefore, increasing the maximum maturity of advances to member banks on their promissory notes secured by such paper would not involve a broadening in the character or class of paper or securities which may be legally acquired by Federal reserve banks and would not constitute in any respect a departure from the fundamental purposes of the Federal Reserve Act.

There is no difference in principle between the rediscount by a Federal reserve bank of paper arising out of an agricultural, commercial or industrial transaction, and an advance to a member bank on its promissory note secured by paper arising out of such a transaction. A member bank which has paper of this kind in its portfolio may use it to obtain credit from its Federal reserve bank by either method. The underlying transaction which is the basis for the credit is, therefore, the same in either case; the substance of the transaction is the same and the only difference is one of form. Furthermore, although it was apparently contemplated by the original Federal Reserve Act that member banks would rediscount paper with the Federal reserve banks to obtain funds with which to finance the transactions giving rise to the rediscounted paper, experience has demonstrated that member banks usually borrow for the purpose of restoring depleted reserve balances with the Federal reserve banks rather than for the purpose of making additional loans; and the purpose of the borrowing is, therefore, the same whether the funds are obtained through re-

discounting or by means of a direct advance from the Federal reserve banks. There is accordingly no logical reason why Federal Reserve Banks should not have the same latitude in making advances to their member banks against the pledge of commercial, industrial and agricultural paper which is eligible for rediscount as they have with respect to rediscounting such paper.

From a practical standpoint, however, the use of promissory notes secured by collateral as a method of obtaining Federal reserve credit has many advantages over rediscounting both for the member banks and for the Federal Reserve banks.

Rediscounting is troublesome and inconvenient. To obtain any substantial amount of credit through rediscounting, a member bank must offer to the Federal reserve bank a number of separate notes or bills of varying amounts and of different maturities; and the amount of discount must be calculated separately for each of these notes or bills. For example, if a member bank wishes to rediscount paper in the amount of $100,000, it is usually necessary for it to offer 50 or 60 or more of its customers' notes for the purpose; and the discount must be separately computed as to each of these notes. If for any reason, other notes are later substituted for some of those first rediscounted the amount of discount on each of the substituted notes must also be calculated. When a member bank borrows on its own promissory note secured by collateral, however, it is only necessary to compute the interest on one note for the full amount of the loan and, in cases of

substitution of collateral, no additional computation of interest is required.

Not only the member banks but the Federal reserve banks as well are benefited by the use of the direct borrowing method in obtaining Federal reserve credit. The amount of interest on each note rediscounted by a member bank must be calculated both by the Federal reserve bank and by the member bank; and a direct borrowing on the basis of one note, therefore, saves the Federal reserve bank much trouble and expense. In addition, it is necessary for the Federal reserve bank to send back to the member bank for collection each note under rediscount as it matures; whereas, the return of notes for collection is unnecessary in the case of an advance to a member bank on its promissory note because the notes or bills pledged with the Federal reserve bank as collateral security do not mature until after the maturity of the advance by the Federal reserve bank. This also results in the saving of much labor on the part of the Federal reserve banks.

Furthermore, in the event of the failure of a member bank which has discounted notes with a Federal reserve bank, it is necessary for the Federal reserve bank to prove a separate claim against the insolvent institution for each note under rediscount; whereas in a case where a Federal reserve bank holds a member bank's own note secured by any number of notes as collateral, it may, in the event of the failure of the member bank, prove one claim for the entire amount.

It was the practice of banks, prior to the enactment of the Federal Reserve Act to borrow from their correspondent banks on their own promissory notes secured by collateral. This form of borrowing from Federal reserve banks, however, was not permitted to member banks by the original Federal Reserve Act; and membership in the Federal Reserve System was less attractive on this account. Many of the banks which were members of the system preferred to continue their practice of borrowing from their correspondent banks on their own promissory notes rather than to change their method of borrowing in order to avail themselves of the rediscount facilities of the Federal Reserve System. By an amendment to the Federal Reserve Act, adopted September 7, 1916, Congress authorized Federal reserve banks to make direct loans to their member banks on their promissory notes secured by paper eligible for rediscount or for purchase by Federal reserve banks or secured by bonds or notes of the United States; but the maturity of such notes was limited to 15 days.

This amendment proved of material benefit to member banks which are located in the same cities with Federal reserve banks or their branches or in nearby cities, and such banks have made extensive use of the privilege of direct borrowing on their promissory notes. Country banks generally, however, have

not availed themselves of this privilege to any great extent because of the inconvenience of renewing their notes every 15 days. The character of business conducted by the larger member banks in financial centers is such that they frequently borrow for only a few days at a time; whereas the character of business of country banks, particularly those in the agricultural sections, is such that they frequently need continuous accommodations for periods extending up to ninety days or more. It is obvious that a bank which needs credit for a period of 90 days will find it decidedly unsatisfactory to borrow on its 15-day note, which would have to be renewed five times during the 90-day period.

To many country banks, therefore, there is available no convenient method of obtaining credit from the Federal reserve banks; and, accordingly, these country banks continue to borrow from their city correspondents on their own promissory notes instead of borrowing from the Federal reserve banks. Borrowing from Federal reserve banks should be made equally as convenient for country banks as for city banks.

It is believed, therefore, that an amendment to the law increasing the maximum maturity of advances to member banks on their promissory notes secured by paper eligible for rediscount or for purchase from 15 to 90 days would be of material benefit both to member banks and to Federal reserve banks, for the following reasons:

1. Rediscounting is necessarily troublesome and in-

convenient to member banks and to Federal reserve banks (a) because of the necessity for calculating separately the amount of discount on each note offered for the purpose, (b) because in cases of substitution of notes interest must be calculated separately on each substituted note, and (c) because each individual note rediscounted must at maturity be returned to the member bank for collection.

2. Borrowing by member banks on their own promissory notes does not involve these difficulties which are present in rediscounting.

3. Under existing law, many country banks do not borrow on their promissory notes because of the inconvenience of renewing such notes every fifteen days; and the proposed amendment would eliminate the necessity for such frequent renewals of member banks' promissory notes and would thus render this method of obtaining credit from Federal reserve banks convenient for use by country banks.

4. A cause of dissatisfaction among country member banks would be removed, and membership in the Federal Reserve System made more attractive to them.

5. In the event of insolvency of a member bank, each note under rediscount for such bank must be proved by the Federal reserve bank as a separate claim, but the entire amount of an insolvent member bank's promissory note secured by collateral may be proved as one claim.

6. An increase in the maximum maturity of direct advances to member banks would not involve any departure from the fundamental purposes of the Federal Reserve Act but would be merely an extension of the principle of the amendment adopted in 1916.

The increase in maturity of advances on member banks' promissory notes should properly be limited to notes which are secured by paper eligible for rediscount or purchase by Federal reserve banks and should not be made applicable to advances secured by bonds or notes of the United States. It is believed that the proposed increase in maturity of notes secured by paper eligible for rediscount or purchase will be adequate to meet the difficulties mentioned above.

Under the existing law, Federal reserve banks are authorized to purchase debentures and other such obligations of Federal Intermediate Credit Banks which have a maturity at the time of purchase of not more than six months. Such obligations of Federal Intermediate Credit Banks are secured by agricultural paper which, when of proper maturities, is eligible for rediscount by Federal reserve banks. In these circumstances it is believed desirable that the law should be amended so as to permit debentures and other such obligations of Federal Intermediate Credit Banks, when complying with the requirements for purchase by Federal reserve banks, to be used as security for advances by Federal reserve banks to member banks on their promissory notes for periods not exceeding fifteen days.

Form No. 131

Office Correspondence

FEDERAL RESERVE BOARD

Date February 3, 1932

To Mr. Goldenweiser

Subject: 15-day notes as an aid to speculation

From Miss Hanford

E.S.H.

O F O 2—8495

I have read carefully the testimony of people directly connected with the Federal reserve system before the subcommittee of the Senate, and also the answers to pertinent questions in the schedules sent out to Federal reserve banks, and I have read more hastily the testimony of other people before this committee.

I have not found any direct admission by anyone connected with the Federal reserve system that 15-day notes collateraled by Government securities are an aid to speculation. In one place, page 149, Senator Glass says: "...my information has been that it (this provision) has been used largely, if not principally, for stock speculative purposes." Later in the course of the hearings, page 258, he says: "As I recall, both Doctor Miller and former Governor Hamlin of the Federal Reserve Board, and very likely--although I am not certain--the Comptroller of the Currency, thought that had been the case." (That such loans had been used for speculative purposes.) I cannot find such references.

I have outlined more completely the discussion of the question and quotations on the subject.

Testimony of Governor Harrison, page 61

In answer to Senator Glass' question: "As a matter of fact, has not that provision of the act (relating to 15-day bills) been very extensively used to increase stock-market operations?" Governor Harrison replies: "I do not know that I would agree with you that that privilege has been used or abused for the purpose of extending accom-

modation for speculative purposes ..." He gives reasons for this view, the chief one being that the use of 15-day notes collateraled by Government securities was simply a matter of convenience and that banks using it could have discounted eligible paper and would have done so except for the fact that rediscounting is a cumbersome process. He does agree (page 62) that "the right of member banks to borrow on Government securities provides an additional mechanism which might be used to further an inflation of the currency." He does not think that this ever takes place, though. He admits that member banks have used "Federal reserve credit as a means of building up their reserves at a time when they have collateral loans, some of which may be used for speculative purposes." The difficulty is in determining when a collateral loan becomes speculative. A speculative use of the proceeds of rediscounting can be made as well as of the proceeds of a 15-day note collateraled by Governments.

Mr. Miller's testimony, page 153 (S 4723, 1930 bill)

" I think it would prove unworkable (Section 11, Glass bill), except at the cost of occasional serious stringencies in the leading money markets of the country." He makes no direct reply to the question of the 15-day notes as an aid to speculation, but the general discussion of this provision implies that he thinks such notes are not an aid to speculation. (page 152) About section 11 of the Glass bill, S 4723 he says: "...on the amendment, with the purpose of which I am in the most complete accord--and by purpose I mean to restrict the use of Federal reserve credit in speculative loans--." He then proposes an emergency proviso by which the restriction would be lifted for a short period.

Mr. Hamlin's testimony, page 180

He thinks that notes secured by Government bonds should be permitted only in an emergency or at a higher rate, though he favors the extension of the use of notes collateraled by eligible paper. He gives no reason for favoring this restriction.

TESTIMONY OF OTHERS

Mr. Davison, President of the Central Hanover Bank and Trust Company of New York, (page 258)

Mr. Davison says that he does not know of an abuse of the 15-day loan on Government securities. It is in this connection that Senator Glass says: "As I recall, both Doctor Miller and former Governor Hamlin of the Federal Reserve Board and very likely--although I am not certain--the Comptroller of the Currency, thought that had been the case." Mr. Davison reiterates his opinion on page 261.

Mr. Mitchell, Chairman of the National City Bank of New York, (page 292) thinks that, with the exception of isolated cases, the 15-day loan against Governments has not been abused.

Mr. Owen D. Young, Chairman of the Board, General Electric Company, (page 362) thinks that "... a situation where Governments may be used as the basis for Federal reserve credit without relation to that yardstick (commercial activity) merely means that they may be used, if the management of the system so elects, to create pools of speculative funds as well as pools of business funds." He does not approve of this.

Mr. Traylor, Chairman of the Board of Directors of the First National Bank of Chicago, (page 405) thinks that the 15-day provision of the Federal Reserve Act has been used for stock speculative purposes no more than any

other form of Federal reserve credit. He thinks there is no way of controlling it.

QUESTIONNAIRE SENT TO FEDERAL RESERVE BANKS filed 332.2-54 dated 2/25/31

Page 716. In answer to question 7 of Questionnaire 7, "Would it assist in preventing Federal reserve credit from being used for speculative and investment purposes to repeal the provision in the Federal Reserve Act permitting member banks to borrow on their 15-day promissory notes secured by Government obligations?"

Eight of the banks said "no." Chicago thought it might in a few cases, Cleveland and Kansas City concurred in this opinion. Dallas said it would undoubtedly assist in accomplishing the purpose. San Francisco (page 720) replied: "It would assist, but not necessarily prevent, the practice because other means are available for obtaining Federal reserve credit surreptitiously." None of the banks favored the provision.

(page 781). In answer to question 12 of Questionnaire 8: "Would the imposition of such discriminatory rates (on notes secured by Governments) help to prevent the seepage of Federal reserve credit into speculative security loans?" Atlanta and Cleveland admitted that it might have some effect. None of the banks favored the provision.

December 3, 1931

Honorable Louis T. McFadden,
House of Representatives,
Washington, D. C.

My dear Mr. Congressman:

In reply to your two letters of November 23, we are enclosing statements showing the aggregate amount of promissory notes of member banks taken by the Federal Reserve banks during the years 1918, 1919 and 1920, and the amount of bills, apart from member bank promissory notes, discounted for member banks by the Federal Reserve banks in the years 1928, 1929 and 1930.

As you know, the maturity of member bank promissory notes taken by the Federal Reserve banks cannot exceed 15 days, whereas commercial paper discounted by Federal Reserve banks may have a maturity at the time of discount of 90 days and certain types of agricultural paper a maturity of not exceeding nine months. In order, therefore, to give you some indication of the amount of accommodation that member banks were actually obtaining from the Federal Reserve banks on each class of paper, we have also shown in the enclosed tables the Federal Reserve banks' holdings of member bank collateral notes on the last Friday of each month during 1918, 1919 and 1920, and their holdings of discounted bills apart from member bank collateral notes on the last day of each month during 1928, 1929 and 1930.

Very truly yours,

(Signed) Chester Morrill

Chester Morrill,
Secretary

(Enclosures)

VF/EMM/fsf

MEMBER BANK PROMISSORY (COLLATERAL) NOTES DISCOUNTED BY FEDERAL RESERVE BANKS FOR MEMBER BANKS IN 1918, 1919 AND 1920.

Volume Discounted

1918	$33,007,788,000
1919	72,548,008,000
1920	55,565,447,000

Holdings of F. R. Banks on Last Friday of Each Month.

	1918	1919	1920
January	$230,079,000	$1,104,345,000	$1,146,631,000
February	144,669,000	1,433,315,000	1,223,220,000
March	160,547,000	1,471,160,000	1,088,157,000
April	510,862,000	1,579,665,000	1,117,605,000
May	474,816,000	1,624,838,000	1,124,643,000
June	366,617,000	1,354,648,000	965,068,000
July	616,369,000	1,398,951,000	962,417,000
August	805,996,000	1,409,543,000	1,021,207,000
September	1,101,769,000	1,375,706,000	933,927,000
October	940,589,000	1,491,707,000	924,821,000
November	1,056,563,000	1,385,343,000	920,778,000
December	1,058,963,000	1,166,020,000	887,417,000

BILLS, OTHER THAN MEMBER BANK PROMISSORY (COLLATERAL) NOTES DISCOUNTED BY FEDERAL RESERVE BANKS FOR MEMBER BANKS IN 1928, 1929 and 1930

Volume Discounted

1928	$1,790,986,000
1929	2,663,187,000
1930	1,030,575,000

End-of-month Holdings of Federal Reserve Banks

	1928	1929	1930
January	$89,507,000	$188,639,000	$138,601,000
February	116,084,000	212,971,000	126,327,000
March	146,830,000	224,311,000	99,740,000
April	160,343,000	248,750,000	106,999,000
May	209,909,000	319,848,000	124,837,000
June	218,789,000	288,821,000	120,014,000
July	244,778,000	296,729,000	115,265,000
August	254,563,000	338,931,000	116,779,000
September	212,588,000	304,026,000	95,250,000
October	208,446,000	275,976,000	99,275,000
November	207,207,000	291,781,000	107,718,000
December	204,924,000	172,896,000	99,302,000

December 3, 1931

Honorable Louis T. McFadden,
House of Representatives,
Washington, D. C.

My dear Mr. Congressman:

In reply to your two letters of November 23, we are enclosing statements showing the aggregate amount of promissory notes of member banks taken by the Federal Reserve banks during the years 1918, 1919 and 1920, and the amount of bills, apart from member bank promissory notes, discounted for member banks by the Federal Reserve banks in the years 1928, 1929 and 1930.

As you know, the maturity of member bank promissory notes taken by the Federal Reserve banks cannot exceed 15 days, whereas commercial paper discounted by Federal Reserve banks may have a maturity at the time of discount of 90 days and certain types of agricultural paper a maturity of not exceeding nine months. In order, therefore, to give you some indication of the amount of accommodation that member banks were actually obtaining from the Federal Reserve banks on each class of paper, we have also shown in the enclosed tables the Federal Reserve banks' holdings of member bank collateral notes on the last Friday of each month during 1918, 1919 and 1920, and their holdings of discounted bills apart from member bank collateral notes on the last day of each month during 1928, 1929 and 1930.

Very truly yours,

(Signed) Chester Morrill

Chester Morrill,
Secretary

(Enclosures)

MEMBER BANK PROMISSORY (COLLATERAL) NOTES DISCOUNTED BY FEDERAL RESERVE BANKS FOR MEMBER BANKS IN 1918, 1919 AND 1920.

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December	1,058,963,000	1,166,020,000	887,417,000

BILLS, OTHER THAN MEMBER BANK PROMISSORY (COLLATERAL) NOTES DISCOUNTED BY FEDERAL RESERVE BANKS FOR MEMBER BANKS IN 1928, 1929 and 1930

Volume Discounted

1928	$1,790,986,000
1929	2,663,187,000
1930	1,030,575,000

End-of-month Holdings of Federal Reserve Banks

	1928	1929	1930
January	$89,507,000	$188,639,000	$138,601,000
February	116,084,000	212,971,000	126,327,000
March	146,830,000	224,311,000	99,740,000
April	160,343,000	248,750,000	106,999,000
May	209,909,000	319,848,000	124,837,000
June	218,789,000	288,821,000	120,014,000
July	244,778,000	296,729,000	115,265,000
August	254,563,000	338,931,000	116,779,000
September	212,588,000	304,026,000	95,250,000
October	208,446,000	275,976,000	99,275,000
November	207,207,000	291,781,000	107,718,000
December	204,924,000	172,896,000	99,302,000

HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING AND CURRENCY

WASHINGTON

November 23, 1931.

Federal Reserve Board,
Washington, D. C.

Gentlemen:

Will you kindly let me know the total amount in dollars advanced by Federal reserve banks on member banks' promissory notes in each of the following years: 1918, 1919, and 1920. This will greatly oblige me.

Very truly yours,

L. T. McFadden

Wm. Lovett

SEVENTY-FIRST CONGRESS

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HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING AND CURRENCY

WASHINGTON

November 23, 1931.

Federal Reserve Board,
Washington, D. C.

Gentlemen:

Please let me know the total amount in dollars of bills discounted by the twelve Federal reserve banks apart from member banks' promissory notes, in each of the years 1928, 1929, and 1930

Very truly yours,

L. T. McFadden

Mr. Snead

November 9, 1931.

Mc F

332.3

Hon. Louis T. McFadden, Chairman,
Committee on Banking and Currency,
House of Representatives,
Washington, D. C.

My dear Congressman:

In reply to your letter of November 2, you are advised that the aggregate amount of 15-day promissory notes of member banks taken by Federal Reserve banks during each of the past three calendar years has been as follows:

1928	$60,598,690,000
1929	58,046,697,000
1930	13,022,782,000

The Board does not have available information as to the amounts originally advanced on member bank promissory notes secured by paper eligible for discount or purchase by the Federal Reserve banks separately from the amounts advanced on notes secured by Government obligations. However, it does have figures derived from reports of the Federal Reserve banks to the Board showing such segregation for member bank promissory notes held by the Federal Reserve banks at the end of each month for the above calendar years, and there is enclosed a table showing such holdings.

Very truly yours,

Chester Morrill,
Secretary.

Enclosure.

END OF MONTH HOLDINGS OF MEMBER BANK PROMISSORY (COLLATERAL) NOTES DISCOUNTED BY FEDERAL RESERVE BANKS

(In thousands of dollars)

Date	Secured by United States Government obligations	Secured by paper eligible for discount or purchase
1928		
January	297,821	35,226
February	306,091	70,279
March	363,439	88,083
April	588,731	84,503
May	708,202	103,046
June	747,577	128,538
July	620,008	165,120
August	661,538	188,471
September	663,982	187,940
October	559,705	152,332
November	733,371	135,323
December	658,242	180,573
1929		
January	499,404	102,201
February	599,453	147,863
March	675,990	181,265
April	515,821	160,376
May	582,577	161,891
June	573,705	168,700
July	591,858	181,566
August	516,141	189,523
September	457,211	192,590
October	524,476	196,017
November	533,906	202,373
December	352,773	105,607
1930		
January	206,933	47,662
February	180,978	45,341
March	171,544	37,864
April	105,666	19,357
May	132,362	54,274
June	108,139	42,968
July	66,201	17,916
August	66,459	30,971
September	105,405	71,296
October	74,082	33,583
November	111,938	53,788
December	88,990	62,299

SEVENTY-FIRST CONGRESS

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HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING AND CURRENCY

WASHINGTON

November 2, 1931.

Federal Reserve Board,
Washington, D. C.

Dear Sirs:

Kindly let me know the total amount advanced to member banks on their 15-day promissory notes secured by collateral eligible for discount or for purchase by Federal Reserve Banks in the years 1928, 1929, and 1930; and likewise the total amount advanced to member banks on their 15-day promissory notes secured by Government paper in the years 1928, 1929, and 1930.

This will greatly oblige me.

Yours very truly,

L. T. McFadden

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-6915

June 19, 1931.

SUBJECT: Action on Governors' Conference Topics.

Dear Sir:

There is attached hereto for your information, copy of a letter to the Secretary of the Governors' Conference, advising of the action taken by the Board on certain of the topics discussed at the Conference held in Washington on April 27-29, 1931.

Very truly yours,

J. C. Noell,
Assistant Secretary.

Enclosure.

TO GOVERNORS OF ALL FEDERAL RESERVE BANKS EXCEPT SAN FRANCISCO.

COPY

X-6915-a

June 19, 1931.

Dear Mr. Strater:

This will acknowledge receipt of your letter of May 26th, enclosing copies of the Secretary's minutes of the Governors' Conference held in Washington on April 27th, 28th and 29th. The Federal Reserve Board has given consideration to the various topics discussed by the Conference and action has been taken as follows:

Topic II-D - Change in weekly Federal reserve bank statement.

The Board has approved the suggestion that the special one-day certificates of indebtedness issued by the Treasury Department to Federal reserve banks to cover Treasury overdrafts on tax payment dates, be shown separately in the body of the weekly Federal reserve bank statement against the caption, "Special Treasury Certificates."

Topic II-E-1 - Payment of a sum equal to one or more months' salary to the widow, dependents, or estate of deceased officers or employees.

In connection with the first recommendation of the conference on this topic, the Federal Reserve Board has ruled that in the event of the death of an officer or employee of a Federal reserve bank, the salary of such officer or employee should be paid only up to the next succeeding pay day.

The Board has not yet acted, however, on the matters of an increase in group insurance for officers and employees at Federal reserve banks, and the establishment of annuity or pension plans by the individual banks.

Topic II-E-2 - Payment of salary in full or in part to officers or employees incapacitated on account of sickness or otherwise.

The Board has noted with approval the action of the Conference in voting that where the absence of officers or employees on account of sickness or other incapacitation exceeds the regular vacation period by thirty days, payment of salary during further leave of absence should be subject to approval by the Board of Directors and reported monthly to the Federal Reserve Board in accordance with the Board's letter of June 14th, 1928, (X-6069).

Supplementary Topic B. - Suggested policy in acting on applications of state banks and trust companies for membership.

The Board has adopted the proposed policy, in connection with its consideration of applications of state banks and trust companies for membership in the Federal Reserve System, that at the time of admission

to membership the applicant bank shall be free from all known losses and depreciation so that on the date its membership becomes effective its statement will reflect as nearly as possible the value of its assets. In this connection, a letter is going forward today to all Federal Reserve Agents, requesting that they bring this action of the Board to the attention of their committees of directors which pass on applications, in order that they may be governed accordingly in making their recommendations to the Federal Reserve Board.

Topic I-D - Desirability of flexibility of interest rates paid on deposits and of bank dividends.

The Board has noted with approval the action and expressions of opinion of the Conference in regard to this topic.

Topic I-F - Possible desirability of amending the Federal Reserve Act so as to permit a Federal reserve bank in emergencies to make advances to member banks on the security of assets other than presently eligible paper.

Action on the resolution adopted by the Conference on this topic has been deferred by the Board for the time being.

Topic II-F - Advertising Federal reserve membership.

The Board has noted with approval the opinion of the Governors that Federal reserve banks could not with propriety give approval or support to any agency or organization soliciting subscriptions from banks and others for the purpose of explaining or advertising the benefits derived from membership in the Federal Reserve System.

No action is required by the Board on the other topics discussed at the Conference or on the various reports submitted by its committees.

A copy of this letter is being forwarded to the Governor of each Federal reserve bank for his information.

Very truly yours,

J. C. Noell,
Assistant Secretary.

Mr. H. F. Strater, Secretary,
Governors' Conference,
Federal Reserve Bank,
Cleveland, Ohio.

1

Data from Call Reports

5430.1

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

January 24, 1930
St. 6470

332.3
33323

Dunder

SUBJECT: Paper Eligible for Rediscount
with Federal Reserve Banks

Dear Sir:

Since October 3, 1928, all member banks have been required to report the amount of loans eligible for rediscount with Federal reserve banks against item 9 in schedule E of the quarterly call report. These figures have been abstracted by the Board and by the Comptroller of the Currency and are now published regularly in the consolidated Member Bank Call Report.

While the published figures show that there is about $4,600,000,000 of eligible paper held by all member banks, no adequate data are available to show the distribution of eligible paper among individual banks or groups of banks in the various sections of the country. The Board believes it desirable to compile such information, also similar information regarding U. S. Government securities which can be used as collateral to member banks' promissory notes. It will therefore be appreciated if you will have compiled and transmitted to the Board the data called for by the accompanying sample form, for each member bank in your district, from the December 31, 1929 call reports.

In order that the information may be tabulated conveniently by states in accordance with certain percentage groupings, it is requested that the figures for each bank be submitted on a separate card, preferably of a size about 4"x 6". In compiling these data it is suggested that, if the amount of eligible paper as reported against item 9 in schedule E is apparently incorrect, the member bank be asked to correct or confirm the figures.

Very truly yours,

Roy A. Young,
Governor

Enclosure

TO ALL F. R. AGENTS*

(Sample form)

F.R.DISTRICT ____ STATE _____

CITY _____ BANK _____

(Amounts in thousands of dollars)

A. Loans, including overdrafts (call report items 1-2)	7,496
B. Loans and investments (call report items 1-4)	10,053
C. Government securities less National bank notes outstanding (call report item 3, less item 20 for National banks)	750
D. Eligible paper (call report item 9 of schedule E)	1,236
E. Eligible paper plus Government securities - net (D + C)	1,986
F. Ratio of eligible paper to total loans	16.5%
G. Ratio of eligible paper, plus Government securities - net, to loans and investments	19.8%

St. 6470

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

April 5, 1929.

Sir:

The Conference of Governors of the Federal Reserve Banks, in considering your letter of March 12th as to the desirability of establishing a higher rate of discount on member bank collateral notes secured by government obligations than is maintained for discounting eligible paper, voted:

"That in the opinion of the Conference, it is not advisable at the present time to establish any differential between these two classes of paper, and if any such differential were to be established, consideration of it should be postponed until after the Federal Reserve banks are ready to reduce their rediscount rates."

Respectfully yours,

W. W. Stralter
Secretary,
Conference of Governors.

Hon. Roy A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

Noted & Action Deferred

April 2, 1929

Would it be desirable to have a spread in the rediscount rate, the lower rates applying to short maturities and the higher rates to long maturities, with the proviso that the highest rate shall apply to member banks collateral notes secured by U. S. Government obligations, and that the rate on member banks collateral notes secured by eligible paper shall be governed by the longest maturity of any of the paper used as collateral?

Yes:-

(1) A range of rates with the existing rate as a minimum, particularly when first established, might enable the System to secure the psychological effect that would follow from an increase in the discount rate without changing appreciably the cost to member banks or their customers of credit for commercial and industrial purposes.

(2) It might convey the impression to the public that the System was ready to advance credit to commerce and industry at a minimum cost consistent with existing conditions but that higher rates should apply to borrowings where the character of the paper did not clearly indicate that the funds borrowed would be used to finance current business.

(3) It would tend to keep the discounts of the Federal reserve banks in the short maturities and thus make changes in the discount rates more promptly effective than if the portfolios were made up of paper of longer maturity.

No:-

(1) It is well nigh impossible to determine from the character of paper on which a member bank borrows the use it makes of the borrowed funds. For this reason it is doubtful whether any worth while results could be accomplished by the differential in rates.

(2) Over 80 per cent of the paper now under discount for member banks has a maturity of not more than 15 days and consequently any changes in discount rates would become effective about as promptly as they would under the above proposal.

(3) Should the Federal reserve banks have a lower discount rate on one class of paper than on another the lower rate would soon become the effective rate on a very large proportion of the borrowings.

(4) The higher rates on the long maturities would discriminate principally against the country bank which would find it difficult to maintain a portfolio of short-time eligible paper sufficient to cover its borrowing requirements at certain times of the year, and against agricultural and livestock paper generally.

(5) A differential in favor of paper of short maturity would undoubtedly result in member banks requiring their customers to borrow on paper of short maturity to their customers' inconvenience and with no real improvement in the character of their portfolios, as the banks would be committed to a renewal of the loans at maturity.

(6) Should the Federal reserve banks have a range of rates and apply the highest rate to member bank collateral notes secured by Government obligations such practice would have a bearish effect on the Government security market and, in my opinion, such effect would be more pronounced than would that of an increase in the present rate which applies to all classes and maturities of eligible paper. If all rediscounts took a uniform rate member banks would consider an increase in rate to be only temporary and would still find it advantageous to use their Governments for borrowing purposes, while if a lower rate were charged on short term rediscounts they would feel that the discrimination against Governments would probably be permanent thus making it no longer profitable to hold them for use as collateral for borrowings at Federal reserve banks. A differential in discount rates adverse to Government secured paper would, therefore, no doubt result in smaller holdings of Government securities by member banks and the replacement of such securities by other earning assets. The advisability of adopting such differentials in rates would seem to depend largely on whether the resulting change in the portfolios of member banks would be a desirable one.

(7) So long as the Federal Reserve Act requires the System to apply the same rate to all member banks rediscounting paper of the same character, I am inclined to believe that there should be one uniform price at which credit may be obtained through discount channels, and that so far as practicable the cost of credit obtained through open market operations should be approximately the same as of credit obtained by rediscounting.

#5

March 14, 1929.

Dear Governor Seay:

This will acknowledge receipt of your letter of March 13th, and I am glad that you expressed yourself the way you have about the subject matter of our circular letter of March 12th, X-6262. After a good deal of hesitancy because of statements that have been made in the past, I recommended to my colleagues that the topic be put on the program of the Governors' conference, and a full discussion will probably disclose whether a higher rate of discount on member bank collateral notes secured by Government obligations is practicable or not.

Some time ago, I wrote you stating that the Board would correspond with the reserve banks in reference to the Federal Advisory Council's recommendation. All of the Federal reserve banks have in one way or another used the statement of the Advisory Council and have advised the Board of their action. Under these circumstances, the Board did not feel that it should go any further. Your procedure is to center your efforts on those banks that you have reason to believe are abusing the rediscount facilities. This method has also been used in other districts with some beneficial results. I am sure the Board would appreciate it very much if, at your convenience, you would advise it of the results you have obtained.

With kind personal regards, I am, as ever

Yours very truly,

(Signed) R. A. Young

R. A. Young,
Governor.

Mr. Geo. J. Seay, Governor,
Federal Reserve Bank,
Richmond, Virginia.

FEDERAL RESERVE BANK
OF RICHMOND

3323

March 13, 1929.

Dear Governor Young:

I am in receipt of your letter of March 12, X-6262, suggesting as a topic of discussion at the coming Conference of Governors the advisability of establishing a higher rate of discount on M. B. C. notes secured by Government obligations than is maintained on eligible paper.

As you say, the matter has been touched upon at some conference of reserve bank officials but only superficially, and never under such conditions as exist as present, of course. It has occurred to us, as probably it has occurred to all Federal reserve bank administrators, but it would need to be considered in all of its aspects, with an interchange of opinion among Federal reserve banks, all of which do not operate under similar conditions. It is undoubtedly true that many banks borrow against Government securities for convenience and use the proceeds just as they would use the proceeds of commercial paper.

The subject is worthy of a great deal of thought.

Very truly yours,

GJS-CCP

GEO. J. SEAY,
Governor.

Honorable R. A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

Re Collateral notes. R. Ritter.

324

332.12

FEDERAL RESERVE BOARD

WASHINGTON

~~332 3~~

3328

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-6262

March 12, 1929.

SUBJECT: Topic for Governors' Conference.

Dear Sir:

There is enclosed herewith copy of a letter which the Board has today forwarded to Mr. H.F. Strater, Secretary of the Governors' Conference, advising that it would like to have discussed at the conference to be held on April 1-3, 1929, the question of the advisability of establishing a higher rate of discount on member bank collateral notes secured by Government obligations than is maintained for discounting eligible paper.

As the time is limited, advice of the placing of this topic on the program of the conference is being forwarded to you direct, and it would be appreciated by the Board if you would come prepared to present your views.

Very truly yours,

R. A. Young,
Governor.

TO GOVERNORS OF ALL F. R. BANKS.

(ENCLOSURE)

COPY

X-6262-a

March 12, 1929.

Boston Bk to Mr McClellan

Dear Mr. Strater:

The Governor of one of the Federal reserve banks has had some correspondence with the Federal Reserve Board as to the desirability of establishing a higher rate of discount on member bank collateral notes secured by Government obligations than is maintained for discounting eligible paper.

If I remember correctly, this question has been discussed by the Governors, at least informally, but the present situation has developed so many unusual angles that some very strong arguments are presented in support of the proposal, in view of which the Board wishes to place the topic on the program for the next Governors' Conference.

Inasmuch as the time is limited, I am today sending a copy of this letter to the Governors of the various Federal reserve banks.

Yours very truly,

(S) R. A. Young,
Governor.

Mr. H. F. Strater, Secretary,
Governors' Conference,
Federal Reserve Bank,
Cleveland, Ohio.

manner to locate org

Minimum requirements
7 days

#12

FEDERAL RESERVE BOARD FILE

~~3323~~

3323

March 12, 1929

Personal & Confidential

Dear Mr. Case:

When you were in Washington the other day you left the enclosed memorandum with me. As I recall, you were not leaving it with me permanently and I am therefore returning it to you herewith.

re minimum maturities 7 days LRC

When it is released, however, I should like very much to have a copy for my files.

Yours,

Mr. J. H. Case,
Deputy Governor,
Federal Reserve Bank,
New York City, N. Y.

FORM No. 131

Office Correspondence

FEDERAL RESERVE BOARD

Date March 1, 1929.

To All Members of the Board

From Mr. McClelland

Subject: 332.3

332.3

0 r o 2—8495

At the meeting this morning, there was ordered circulated the attached letter dated February 25th from the Governor of the Federal Reserve Bank of Boston with reference to the eligibility of member bank fifteen day notes secured by Government obligations as collateral for Federal Reserve notes.

Governor Young
Mr. Platt
Mr. Hamlin
Mr. James
Mr. Cunningham
Mr. Miller
Mr. Pole

Please circulate promptly and return to the Secretary's Office.

332

FEDERAL RESERVE BANK
OF BOSTON

W. P. G. HARDING
GOVERNOR

March 1, 1929

Dear Governor Young:

I have received your letter of the 27th instant and am obliged to you for sending me a table showing the effect upon the various Federal reserve banks at the present time, if the Board should decline to permit them to use member banks' collateral notes secured by government obligations as security for Federal reserve notes.

I note that you think that the questions raised in my letters would be interesting topics for the forthcoming governors' conference, and I would suggest that if they were proposed by the Federal Reserve Board, they would receive more serious consideration than would be the case if they were proposed by me.

Very truly yours,

Governor.

Hon. Roy A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

J

3323

February 27, 1929.

Dear Governor Harding:

As I advised you over the telephone today, I have discussed with my colleagues your suggestion that commercial, industrial and agricultural rates be maintained at a lower rate than fifteen day collateral notes secured by Government obligations. While no commitments were made by my colleagues, I think I can say to you with safety that they are giving serious consideration to your proposal.

2/27/29

I have also acquainted them with the contents of your letter questioning the eligibility of fifteen day collateral notes secured by United States Government bonds. As to collateral security for Federal reserve notes, I have not asked for any written legal opinion in reference thereto, but our Counsel has stated to me informally that he believes there is no question about their eligibility. In your telephone talk today you put forth the suggestion that the Board could properly refuse such notes as collateral security for Federal reserve notes from a legal standpoint, and while I am inclined to agree with you, the question arises as to whether this would be advisable or not.

I have had Mr. Smead prepare a table which I am sending herewith showing the effect upon the various reserve banks at the present time if this procedure were adopted. You will observe in the last column that some of the reserve banks would have pretty low reserves. All of these could be adjusted by shifting United States Government securities, with the exception of Atlanta. If our figures are accurate and they should shift their United States Government securities, their reserve percentage would only be 17.2%, which would necessitate their rediscounting with other Federal reserve banks approximately $12,000,000.

Both of your letters bring up some very interesting questions and it seems to me that these would both be very interesting topics for the forthcoming Governors' Conference.

With kind personal regards, I am

Yours very truly,

(Signed) R. A. Young

R. A. Young,
Governor.

Mr. W. P. G. Harding, Governor,
Federal Reserve Bank,
Boston, Mass.

(Enclosure)

Form No. 131

Office Correspondence

FEDERAL RESERVE BOARD

Date February 26, 1929

To Governor Young

Subject: 3323

From Mr. Smead

ere 2—8495

R. A. Y. FEB 27 1929

In accordance with your request of this morning I am handing you herewith a statement showing what the effect would be on the Federal reserve banks if member bank collateral notes were ruled to be ineligible as collateral security for Federal reserve notes.

As I stated this morning, the only material effect such ruling would have on Federal reserve banks at this time would be to reduce the amount of gold and lawful money available as reserves against deposits at a number of the Federal reserve banks below the 35 per cent minimum required by law. From the attached table you will see that the deposit reserves of five of the banks would be less than 35 per cent. Such reserves could, however, be raised above the 35 per cent level at all banks except Atlanta by the sale to other Federal reserve banks of U. S. securities held in the special investment account or in their regular investment portfolio. In the case of the Atlanta bank the reserve ratio would be only 17.2 per cent after the sale of all of its U. S. securities. Atlanta would, in fact, have to rediscount $12,000,000 of member bank collateral notes with other Federal reserve banks in order to bring its deposit reserve up to the 35 per cent minimum.

If member bank collateral notes were ruled to be ineligible as collateral for Federal reserve notes, no doubt a substantial proportion of the borrowings at certain of the Federal reserve banks which are now in the form of member bank collateral notes would be converted into rediscounts and, of course, if this were done on a large scale it would leave the banks in substantially the same position as they now are. As a matter of fact, the Federal Reserve Bank at Boston still follows the practice adopted during the war of rediscounting eligible paper for member banks under a fifteen day repurchase agreement instead of making advances to member banks on their fifteen day collateral notes secured by eligible paper.

Each member of the Board has been furnished with a copy of Mr. Smead's tabulation.

B

FEDERAL RESERVE BANK
OF BOSTON

W. P. G. HARDING
GOVERNOR

3323

February 25, 1929

Dear Governor Young:

In the first paragraph on page 2 of the other letter which accompanies this, you will note that I say - "A Federal reserve bank can use its rediscounted paper as security for Federal reserve notes while it is questionable whether it should use member banks' collateral notes in this way." I know that it is the custom for Federal reserve banks to use member banks' collateral notes secured by government obligations as security for Federal reserve notes, but I have serious doubts whether it was the intent of Congress that such notes should be used in this way. In the first place, none of the government obligations issued during the War or since, have the circulation privilege and where a Federal reserve bank uses a member bank's note secured by such obligations as collateral for Federal reserve notes, it is using a government obligation indirectly in a way where it is clear that it could not make such use of it directly.

Section 13 of the Federal Reserve Act as originally enacted, contained no provision for advances to member banks on their fifteen day collateral notes, and Section 16 of the original Act which relates to Federal reserve note issues, contains this language:

> "The collateral security thus offered shall be notes and bills, accepted for rediscount under the provisions of Section thirteen of this Act, and the Federal Reserve Agent shall each day notify the Federal Reserve Board of all issues and withdrawals of Federal reserve notes to and by the Federal reserve bank to which he is accredited."

In the amendment to the Federal Reserve Act approved September 7, 1916, the following paragraph was inserted in Section 13:

> "Any Federal reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal reserve bank, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States."

Ordered circulated

In the same Act of September 7, 1916, Section 16, paragraph 2, relating to note issues was amended as follows:

> "Any Federal reserve bank may make application to the local Federal reserve agent for such amount of Federal reserve notes hereinbefore provided for as it may require.....
> The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances rediscounted under the provisions of Section thirteen of this act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of Section fourteen....."

It is clear that under the original Act, fifteen day collateral notes could not be used as security for Federal reserve notes for there was no provision permitting Federal reserve banks to acquire such collateral notes. It seems to me that it is equally clear that under the act of September 7, 1916, which permitted Federal reserve banks to take fifteen day collateral notes from their member banks that the amendment to Section 16 above referred to specifically precludes the use of such notes as security for Federal reserve notes for they were not "rediscounted." However, in the amendment to the Federal Reserve Act approved June 21, 1917, Section 16, paragraph 2, was amended by striking out the word "rediscounted" and substituting the word "acquired" so that this section now reads -

> "The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances acquired under the provisions of Section thirteen of this Act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of Section fourteen of this Act.....
> The said Federal Reserve Board may at any time call upon a Federal reserve bank for additional security to protect the Federal reserve notes issued to it."

The substitution of the word "acquired" for the word "rediscounted" has been taken as authorizing the use of member banks' fifteen day collateral notes as security for Federal reserve notes, but in view of the fact that the original act provided that the collateral security thus offered shall be -

> "Notes and bills accepted for rediscount under the provisions of Section thirteen of this Act"

and that the amendment of September 7, 1916 provided that the collateral security thus offered shall be

> "Notes, drafts, bills of exchange or acceptances rediscounted under the provisions of Section thirteen of this Act"

it is my belief that the intent of Congress was merely to provide that any bills of exchange or acceptances which were "acquired" or bought in the open market and not necessarily rediscounted could be used as collateral security for Federal reserve notes.

You will note that there is no direct reference in the amendment of June 21,1917 to Section 16, which is the present law, to member banks' collateral notes, and the only possible authority for the use of such notes as collateral for Federal reserve notes is to have them included in the word "notes" which precedes the words "drafts, bills of exchange or acceptances." As the amendment is so specific in describing the collateral it seems to me that had Congress intended to include member banks' fifteen day collateral notes it would have done so in plain language.

In the original Act reference is made only to notes and bills accepted for rediscount. In the amendment of September 7, 1916, the reference is to "notes, drafts, bills of exchange, or acceptances rediscounted under the provisions of Section thirteen of this Act" and in the amendment of June 21, 1917, the reference is to "notes, drafts and bills of exchange, or acceptances acquired under the provisions of Section thirteen of this Act."

Under Section 13 of the Act as originally passed, any Federal reserve bank

> "may discount notes, drafts and bills of exchange arising out of actual commercial transactions, etc."

There was then no provision for member banks' fifteen day collateral notes. In Section 13 as it now stands, the language is identical, and two pages further on may be found the provision that any Federal reserve bank

> "may make advances to its member banks on their promissory notes for a period not exceeding fifteen days, etc."

As the amendment of June 21, 1917 goes into detail as to the kind of security which may be used and does not mention member banks' fifteen day notes, it seems to me that it is some stretch of the imagination to include them in the word "notes" which word has always occurred immediately before the word "drafts" from the very beginning.

It appears that close reading of the Act seems to preclude the inclusion of the specific term "member banks' fifteen day collateral notes" in the above term "notes" which is used just before the words "drafts and bills of exchange," for paragraph (d) of Section 14 provides that every Federal reserve bank

> "shall have power to establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal reserve bank for each class of paper, which shall be fixed with a view of accommodating commerce and business"

while in Section 13 appears the provision that any Federal reserve bank

> "may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board, etc."

If it was not intended to make a distinction between these member bank collateral notes and ordinary commercial notes, why should there be a separate provision for rates on these notes as distinguished from the ordinary notes which are covered in paragraph (d) of Section 14?

This, of course, is only a layman's opinion; but if the Board should decide to submit this question to counsel, and should counsel give an opinion which would justify a ruling that member banks' collateral notes may not be used as security for Federal reserve notes, I think considerable headway would be made in solving the problems which now confront the Federal Reserve System.

Very truly yours,

Governor.

Hon. Roy A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

J

3323

February 22, 1929

Dear Mr. Case:

You will recall someone suggested, about a year ago, that the minimum maturity on member bank collateral notes be made seven days. This suggestion was referred to the Advisory Council and the Governors, and was turned down unanimously for many reasons which I shall not attempt to repeat in this letter.

I had a talk with Mr. Kenzel the other afternoon and he seemed to be convinced that the seven-day minimum maturity collateral note could be used to advantage. The time was limited and I did not have an opportunity to get all of his views. Since I returned I have thought the matter over and still believe a seven-day minimum maturity would probably do more harm than good. Mr. Kenzel, however, seemed to be so positive in his views that he may have something in mind that we are missing.

At your convenience, would you mind discussing the matter with him and advising me of your reaction?

With kind personal regards, I am

Yours very truly,

(Signed) R. A. Young,

R. A. Young,
Governor.

Mr. J. H. Case,
Deputy Governor,
Federal Reserve Bank,
New York City, N. Y.

#1

327
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332 3
332 3

December 14, 1928.

Dear Mr. Hichborn:

I acknowledge receipt of and thank you for your letter of the 1st instant, advising the Board of the resolution adopted at the meeting of the stockholders of the Federal Reserve Bank of Boston, held November 9, 1928. You have been correctly informed that the Board has decided not to adopt the suggestion that it fix a minimum maturity of seven days for member banks' fifteen day promissory notes.

As to the recommendation contained in the Board's Report to Congress for the year 1927 that the Act be amended so as to permit the reserve banks to make advances to member banks on their promissory notes running for a period of not more than ninety days, I would state that the Board is still interested in securing the necessary legislation and at the appropriate time will renew its recommendation to Congress.

Very truly yours,

(Signed) R. A. Young

R. A. Young,
Governor.

Mr. Charles S. Hichborn, Chairman,
Stockholders Advisory Committee,
c/o The First National Granite Bank,
Augusta, Maine.

Minimum maturity on member call notes 1 year 7 days

324

FEDERAL RESERVE BOARD

WASHINGTON

332.3

332 3

ADDRESS OFFICIAL CORRESPONDENCE TO THE FEDERAL RESERVE BOARD

X-6191

December 10, 1928.

SUBJECT: Action on Conference Recommendations.

Dear Sir:

There are enclosed herewith, for your information, copies of letters addressed to the Secretary of the Governors' Conference and the Chairman of the Conference of Federal Reserve Agents, with respect to the status before the Board of the various matters considered by either or both of the Conferences.

Very truly yours,

Walter L. Eddy,
Secretary.

TO ALL GOVERNORS AND FEDERAL RESERVE AGENTS.

Indexed copy filed 324. 11-14-28

COPY X-6191-a

December 6, 1928.

Dear Governor Harrison:

The Federal Reserve Board has given careful consideration to the various topics discussed at the recent conference of Governors of the Federal Reserve Banks, as reported to it in the Secretary's minutes which you forwarded to the Board under date of December 1, 1928. The status here of the various matters, as well as definite actions which have been taken with respect to some of them, are as follows:

Topic I-a- Suggested revision of Open Market Investment Procedure.
The Board still has this matter under advisement and consideration is being given to the recommendation of the Governors, as amended and adopted by the Joint Conference of Governors and Federal Reserve Agents. The matter will be made the subject of a communication to all Federal Reserve Banks at a later date.

Topic I-b - Discount rates and open market policies.
The Board noted that the Conference appointed a Committee to make a study and to report to each Governor as soon as practicable any conclusions or recommendations which the Committee deems necessary with respect to Federal Reserve credit operations, objectives and policies. It is requested that you arrange to have a copy of the Committee's report forwarded to the Board at the time it is submitted to the Governors.

Topic I-c - Loans by Federal Reserve Banks to their member banks.
The Board concurs in the recommendation of the Conference, made after discussion of the several related subjects listed under this general topic, that it would be advisable to require all reporting member banks each week to report in the same manner now required of banks in some of the principal cities, the amount of their call and time loans to brokers and dealers, secured by stocks and bonds. At an early date appropriate instructions will go forward to all Federal Reserve Banks.

Topic I-c-5 - Minimum maturity on member bank collateral notes.
Upon further consideration of the suggestion contained in the Board's letter of September 4, 1928 (X-6124) relative to the establishment of a minimum maturity on member banks' collateral notes, the Board voted not to adopt the suggestion.

Topic I-c-6 - Suggestion that special effort be made to impress upon member banks the desirability of maintaining adequate portfolios of eligible paper and acquainting them with the kinds of paper eligible for rediscount (Board's letter of August 24, 1928 - X-6118).

The Board has voted to adopt the recommendation made by the Conference that it issue a statement in the Federal Reserve bulletin dealing with the above question and an appropriate statement is in the course of preparation and will appear in an early issue of the bulletin.

Topic I-d - Report on relations with foreign banks.

In the minute entry relating to this topic the statement is made that in addition to your review of the various matters relating to operations of foreign banks of issue, you reviewed plans which are now pending for the stabilization of certain currencies abroad. The minutes do not indicate whether or not this report was a written one, and members of the Board have requested that if a written report was not prepared, copy of which can be forwarded to the Board, you furnish the Board with a memorandum setting forth in substance your remarks concerning the various matters, particularly those relating to stabilization plans which are pending at this time.

Topic IV-a - Proposed revision of functional expense report.

The Board noted the concurrence of the Conference in the views set forth in the report submitted by Messrs. Smead and Rounds, and has voted to approve their recommendation that the functional expense report be continued in its present form.

Topic IV-b-1 - Separate financial statements of corporations or firms closely affiliated with the borrower.

The Board noted the view of the Conference that inasmuch as the relative provisions of Regulation A were amended only recently, it would be preferable as a practical matter not to suggest another amendment to the regulation pending further experience.

Topic IV-b-2 - Desirability of amending Sections 7 and 9 of Regulation A so as to except from the prohibition on the discount of paper bearing the signature or endorsement of nonmember banks, bills of exchange payable at sight or on demand of the kind described in Section 7 (Board's letter X-6145 dated September 26, 1928).

In view of the understanding had at the Joint Conference on November 16th, that the situation giving rise to this question can be handled under the regulation as it now stands, it was voted that no amendment to the regulation be made at this time.

Topic IV-b-3 - Right of Federal Reserve Bank to charge items to the reserve account of banks "at any time when in any particular case such Federal Reserve Bank deems it necessary to do so." (Section 5 Regulation J)

The Board has voted to amend Section 5 of Regulation J by eliminating from paragraph 4 thereof the phrase "Provided, however, that any Federal Reserve Bank may reserve the right in its check-collection circular to charge such items to the reserve account or clearing account of any such bank at any time when in any particular case the Federal Reserve Bank deems it necessary to do so." This amendment will not be made effective, however, until after consultation with the various Federal Reserve Banks.

Topic IV-c - Deduction of foreign balances in computing member bank reserves - (Board's letter X-6125 dated September 4, 1928.)

The views of the Conference on this topic were noted and the Board voted that the ruling made by it in 1919, to the effect that balances due from foreign banks may not be deducted from balances due to other banks by a member bank in calculating its reserves, should not be revoked.

Topic IV-d - Suggestion that meetings between the Federal Reserve Board and the directors of the Federal Reserve Banks be held annually in Washington. (Board's letter X-6142 dated September 22, 1928).

The Board concurs in the position of the Conference that no further action is necessary on this question.

Topic IV-e - Report of Leased Wire Committee.

The summary appearing in the Secretary's minutes relating to this report was noted and the Board will request the Chairman of the Committee to furnish it with a copy of the report for its records.

Topic IV-g - Report of Pension Committee.

The action of the Conference in voting to accept this report was noted and the Board requests that it be furnished at this time with a complete copy of the report for its files and, later, with a copy of the new bill which the Committee plans to offer.

Topic IV-h - Report of Subcommittee of General Committee on bankers' acceptances.

The action of the Conference in approving this report and its instructions to the Committee were noted by the Board, which requests that a complete copy of this report also be furnished to it.

Topic III-b - Future policy with respect to Gold certificate circulation.

The Board concurs in the view of the Conference that no change should be made in the present policy under which gold certificate circulation has been maintained at about one billion dollars.

Topic V-b - Collateral for war loan deposits.

The Board noted with approval the recommendation to be made by the Conference to the Secretary of the Treasury that it would be advisable to make only government securities eligible as collateral for war loan deposits.

Canadian Currency.

For the purpose of making a further study and report on this question the Board has appointed a Committee consisting of Managing Director Schneckenburger of the Buffalo Branch, Managing Director Cation of the Detroit Branch, Managing Director Shaw of the Seattle Branch and Deputy Governor Moore of the Federal Reserve Bank of Minneapolis. The Board later will make this matter the subject of special communications to the Governors of those Federal Reserve Banks having representatives on the Committee.

Governor Harrison....4

Granting of fiduciary powers to national banks (Memo X-6172 dated November 3, 1928.)

The Board noted that the Conference was favorably inclined to the suggestions contained in the memorandum but is not prepared, however, to immediately take definite action with respect thereto. The Board will advise all Federal Reserve Banks in due course of whatever action is taken.

Waiver of six months' notice by state banks voluntarily withdrawing from the Federal Reserve System.

In accordance with the recommendation of the Conference the Board voted to suggest an amendment, at the proper time, which would give it the option of waiving the six months' notice required of state member banks voluntarily withdrawing from the system. If the amendment is passed the reserve banks will be given an opportunity to express to the Board in each individual case their views with respect to the wisdom of a waiver of notice.

The several other matters covered in the Secretary's report do not appear to require any action by the Federal Reserve Board.

Copy of this letter will be forwarded to the Governor of each of the Federal Reserve Banks for his information.

Very truly yours,

R. A. Young,
Governor.

Mr. George L. Harrison, Secretary,
Governors' Conference,
Care Federal Reserve Bank,
New York, N. Y.

COPY

X-6191-b

December 8, 1928.

Dear Mr. Martin:

The Federal Reserve Board has considered the various topics discussed at the recent Conference of Federal Reserve Agents, as reported in the Secretary's minutes forwarded to the Board with your letter of November 28, 1928.

The status here or action taken on the several topics considered jointly by the Federal Reserve Agents and the Governors are reported in a letter dated December 6th to the Secretary of the Governors' Conference, copy of which is enclosed herewith. The other matters discussed by the Federal Reserve Agents were dealt with by the Board as follows:

Topic I-a - Suggestion that special effort be made to impress upon member banks the desirability of maintaining adequate portfolios of eligible paper and acquainting them with the kinds of paper eligible for rediscount. (Board's letter X-6118, dated August 24, 1928.)

In addition to the action of the Board reported in the attached letter to the Secretary of the Governors' Conference in approving the suggestion that a statement on this question be published in the Federal Reserve bulletin, the Board will confer with the Comptroller of the Currency, as recommended by the Federal Reserve Agents, with a view to having his examiners cooperate in the matter of acquainting officers of national banks with eligibility requirements.

Topic I-f - Classification of member banks by electoral groups.

The Board noted the view of the Conference that the classification and grouping must be determined by the needs of each individual district. The replies to the Board's letter of October 12, 1928, X-6159, requesting certain information and suggestions are now being compiled and will be ready for submission to the Board shortly after the first of the year. At that time the Board will again communicate with the Chairman regarding this subject.

Topic I-k - Examination of state member banks (Memo. X-6173 dated October 12, 1928.)

The Board has voted to abolish its Department of State Bank Examinations, effective Febraury 1, 1929. In due course a special communication with reference to this action will be addressed to each Federal Reserve Agent.

Topic I-k - Applications for reduction in reserve requirements. (Memo X-6176, dated October 27, 1928)

The Board has noted the recommendation of the Federal Reserve Agents' Conference on this topic but is not prepared to take immediate action relative thereto.

Topic II-c - Report of Bank and Public Relations Committee.

The action of the Conference in accepting this report has been noted by the Board but no action relative to it will be taken at this time.

Topic II-d - Report of Committee on National Summary of Business Conditions.

The recommendation contained in this report and adopted by the Conference that efforts be made to standardize the length of the summary at about 700 words has been noted and the matter has been referred to the Director of the Board's Division of Research and Statistics.

Topic III-e - When such a thing as a run occurs, how should officers of Reserve Banks and Branches answer questions?

The Board has noted with approval the view of the Conference with respect to the position which should be taken by Federal Reserve Banks and Branches in replying to inquiries regarding bank disturbances.

Topic III-g - Unretired stock in Federal Reserve Banks held by banks in process of liquidation.

In its last annual report the Board recommended an amendment to the Act permitting the cancellation of Federal Reserve Bank stock held by member banks which have gone out of business without a receiver or liquidating agent having been appointed therefor, and has now requested its Counsel to prepare a specific form of amendment which will be considered by the Board in due course.

Topic III-n - Auditing Departments.

The Board approved the action of the Conference in voting that a meeting of the General Auditors of the twelve Federal Reserve Banks and a representative of the Federal Reserve Board be called in the near future for the purpose of discussing problems incident to their work. Mr. Smead will represent the Board at this Conference and it is requested that you communicate with him regarding the time at which it should be held.

The other matters reported in the Secretary's minutes do not require action by the Board.

A copy of this letter and enclosure is being forwarded to the Chairman of each Federal Reserve Bank for his information.

Very truly yours,

R. A. Young,
Governor.

Mr. Wm. McC. Martin, Chairman,
Federal Reserve Agents' Conference,
care Federal Reserve Bank,
St. Louis, Missouri.

STOCKHOLDERS ADVISORY COMMITTEE

FIRST FEDERAL RESERVE DISTRICT

332.3

Augusta, Maine, December 1, 1928.

Federal Reserve Board,
Washington,
D. C.

Gentlemen:-

The following is a copy of a resolution adopted at the meeting of the Stockholders of the Federal Reserve Bank of Boston, which was held on Friday, November 9, 1928:-

"WHEREAS, it has come to the knowledge of member bankers in the First Federal Reserve District that the suggestion has been made to the Federal Reserve Board that the Board's Regulations be amended so as to fix seven days as the minimum limitation on advances by Federal Reserve Banks to member banks on their promissory notes, the effect of which amendment would be to deprive member banks, which have secured advances on such notes, of the privilege of making payment prior to the maturity of such obligations unless with the payment of at least seven days' interest,

AND WHEREAS, advances of this kind are used by most of the larger banks to make good temporary deficiencies in reserve, and are usually repaid within one or two days,

AND WHEREAS, the requirement of interest on such advances for at least seven days would practically compel banks so borrowing to make use of temporary surplus funds in some other manner than the payment of debt to the Federal Reserve Bank, and would encourage, if not compel, the employment of such funds in the call money market,

RESOLVED, that this meeting go on record as expressing the opinion that the regulation suggested would be ill advised and would be injurious, and the Federal Reserve Board is hereby respectfully requested to make no change of the character proposed.

RESOLVED FURTHER that this meeting also go on record as endorsing the proposal made by the Federal Reserve Board in its annual report for the year 1927, that that part of Section 13 of the Federal Reserve Act relating to advances by Federal Reserve Banks to member banks on their promissory notes for a period not exceeding fifteen days, provided such promissory notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal Reserve Banks, or by the deposit or pledge of bonds or notes of the United States, be amended so as to permit such notes to be made for a period of not more than 90 days."

A meeting of the Stockholders' Advisory Committee was held at the bank on November 28,1928 and I was requested by the Committee to transmit a copy of the foregoing resolution to you.

You will note that the resolution was prompted by the proposal which we were informed was made to the Federal Reserve Board some time ago that the Board's regulations be amended so as to fix a minimum maturity of seven days on member banks' 15-day promissory notes.

Since the meeting of the Stockholders' Advisory Committee I have learned that the Board has decided not to make any such change in its regulations and so far as that part of the resolution is concerned I presume the matter may be said to be closed, and there is no occasion on that account for the transmission of the resolution.

However, the latter part of the resolution deals with a different aspect of member banks' promissory notes, that is the desirability of increasing their maximum maturity and because the resolution constitutes an endorsement of the proposal made by the Federal Reserve Board in its annual report for 1927 suggesting an amendment of the Federal Reserve Act to permit such notes to have a maturity of not more than 90 days, I am sending you the resolution in full for your information.

Very truly yours,

D. Richardson

Chairman.

A.

Form No. 131

Office Correspondence

FEDERAL RESERVE BOARD

Date November 20, 1928.

To Governor Young

Subject: 332.3

From Mr. Eddy.

332.3 OPO 2—8495

X-6124 9/4/28

The question of an amendment to the Board's regulations which would fix seven days as the minimum limitation on advances by Federal reserve banks to member banks on their promissory notes secured by eligible paper and government securities (X-6124 - September 4, 1928) was submitted to the recent Conferences of Governors and Federal Reserve Agents.

It was voted to be the sense of the Governors' Conference that

> "Inasmuch as it appeared to the Conference that the establishment of a minimum maturity would fail to accomplish the purposes desired, no change should be made in the present procedure or regulations regarding the discount of such collateral notes."

The Federal Reserve Agents' Conference was also opposed to the suggestion.

At the meeting of the Board on November 15 attention was called to the fact that the matter was also submitted at the last meeting of the Federal Advisory Council and disapproved by that body. Accordingly, upon motion, the suggestion was disapproved by the Board.

9/28/28

133-324

TOPIC NO. 5. Suggest[illegible] that the Board's Regulations [illegible] amended so as to fix seven days as the minimum limitation on advances by Federal Reserve banks to member banks on their promissory notes secured by eligible paper or Government securities.

FEDERAL RESERVE BOARD

3
332

X-6124
332 9/4/28

9/28/28

RECOMMENDATION: The Federal Advisory Council is opposed to the above amendment of the Board's Regulations. It seems to the Council it will tend to increase rather than diminish the funds available for speculation and to increase the sale and purchase of Federal Reserve funds. It is obvious that, if a member bank must borrow for a period of seven days even though it needs the money for a shorter period only, such a bank will be compelled either to place its idle funds temporarily at the disposal of the call money market or to sell such Federal funds to some other member bank.

#1

3324

FEDERAL RESERVE BOARD FILE

~~3323~~

3323

X-6124

September 12, 1928

Dear Governor Harding:

I acknowledge receipt of your letter of September 6th, and thank you for the expression it contains of your views regarding the suggestion that the Board's Regulations be amended so as to fix seven days as the minimum maturity on advances by Federal reserve banks on member bank collateral notes.

You are advised that there will be no objection to your bringing the question up for discussion at your forthcoming stockholders' meeting.

Very truly yours,

(Signed) R. A. Young

R. A. Young,
Governor.

Mr. W. P. G. Harding, Governor,
Federal Reserve Bank,
Boston, Mass.

FOR SPECIAL CIRCULATION

PLEASE READ PROMPTLY, INITIAL AND RETURN TO SECRETARY'S OFFICE

Gov. Young ✓ Mr. Hamlin Mr. James ✓ Mr. McIntosh ✓

Mr. Platt Mr. Cunningham ✓

3323

FEDERAL RESERVE BANK OF BOSTON

September 6, 1928

Hon. Roy A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

See 9/14/28 X-6124

Dear Governor Young:

With reference to Mr. Vest's memorandum regarding a possible regulation by the Board fixing a minimum of 7 days on member banks' 15 day notes which the Board proposes to bring to the attention of the approaching conference of Federal Reserve Agents and Governors, I wish to say that my first reaction to the suggestion is unfavorable.

I notice that Mr. Vest takes the position that the Board has authority to make a resolution of this kind. Without undertaking to question the correctness of his opinion, I wish to call attention to the quotation which he makes from a letter I sent to Senator Owen at the time the amendment was suggested, and to say that the suggestion was made following representations from some of the large banks in New York and other cities that they frequently had occasion to borrow money for one or two days to make good deficient reserves, and that they frequently did not have eligible paper of such short maturities.

I am of the opinion that if the idea of having the Board issue such a regulation is based upon the stock market situation in New York, the effect would be just the opposite from what is intended.

In this district, our country banks frequently renew their 15 day notes from time to time, but the city banks as a rule take such notes up in from one to three days. Should they be obliged to pay us interest for 7 days on any such paper, the result would be that instead of paying us they would loan the money on call in New York until the end of the 7 day period. As a case in point, one of our large banks on yesterday borrowed four million dollars from us on government securities to prevent what otherwise would have been a deficiency in its reserve. Today the note was paid. Had the proposed 7 day rule been in effect, this particular four million dollars would have been loaned on call in New York until the expiration of the 7 day period.

Our stockholders meeting will probably be held on Friday, November 9, and I am writing to ask if the Board would have any objection to having this matter brought up for discussion at that meeting. If it should be presented, we would have an opportunity of ascertaining the banking sentiment in this district toward the proposition.

Very truly yours,

Governor.

J

No objection

AT EXECUTIVE COMMITTEE MEETING,

SEP 12 1928

Dist's memo attached

324
252

FEDERAL RESERVE BOARD

WASHINGTON

332 .3
332.3

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-6124

Carded

September 4, 1928.

SUBJECT: Topic for Joint Conference - Minimum maturity on member bank collateral notes.

Dear Sir:

There is enclosed herewith copy of a memorandum from the Board's General Counsel submitting and commenting upon a proposed amendment to the Board's regulations which would fix seven days as the minimum limitation on advances by Federal Reserve banks to member banks on their promissory notes secured by eligible paper or Government securities. Such an amendment has been suggested as a possible means of preventing day to day borrowings by member banks for the making of loans of a speculative character, and the Board has voted, before acting upon the suggestion, to refer it to the forthcoming conference of the Governors and Federal Reserve Agents for discussion and recommendation, as well as to the fall meeting of the Federal Advisory Council.

Very truly yours,

E. M. McClelland,
Assistant Secretary.

TO ALL GOVERNORS AND
FEDERAL RESERVE AGENTS.

Copy filed 252-A

(COPY)

X-6124-a

FEDERAL RESERVE BOARD

June 21, 1928.

To Federal Reserve Board

From Mr. Vest, Assistant Counsel.

SUBJECT: Minimum maturity of seven days on member banks' collateral notes.

In accordance with the Board's request there has been prepared and is attached hereto a draft of an amendment to the Board's regulations which would fix seven days as the minimum limitation on advances by Federal reserve banks to member banks on their promissory notes secured by paper eligible for rediscount or by bonds or notes of the United States.***

Some question may be raised as to the Board's authority to prescribe a regulation of this kind. In my opinion the Board has the authority under the law to do this if it so desires.

Section 13 of the Federal Reserve Act contains the following paragraph:

> "The discount and rediscount and the purchase and sale by any Federal reserve bank of any bills receivable and of domestic and foreign bills of exchange, and of acceptances authorized by this Act, shall be subject to such restrictions, limitations, and regulations as may be imposed by the Federal Reserve Board."

This provision obviously gives broad authority to the Federal Reserve Board in the matter of regulating the discount and purchase of paper by Federal reserve banks. The term "bills receivable" includes promissory notes, bills of exchange or other instruments for the payment of money. (see WORDS AND PHRASES and Bouvier's LAW DICTIONARY.) This provision of law, therefore, makes the discount of any promissory note by any Federal reserve bank subject to such restrictions, limitations and regulations as may be imposed by the Federal Reserve Board. The broad authority to impose any restrictions and limitations thus given in my opinion empowers the Board to prescribe a minimum limitation on maturity of notes <u>discounted</u> by a Federal reserve bank.

The word "discount" according to the decided cases applies not only to the purchase of a note from one who actually owns the same, i.e., the payee or the holder, but also includes the transaction by which the loan is made to the maker of a note by the payee thereof. See Fleckner v. Bank, 8 Wheat. 338; National Bank v. Johnson, 104 U.S. 271; Esten v. Third National Bank (Ky.), 42 S.W. 1115; and Morris v. Third National Bank (C.C.A.) 142 Fed. 25. In this connection it may be well to mention the fact that the same amendment to the law, that of September 7, 1916, which authorized Federal reserve banks to make advances on member banks' collateral notes, also inserted the words "discount and" in the above quoted paragraph of Section 13. This may be regarded as of some significance as to the intention of Congress.***

I am, therefore, of the opinion that the above quoted paragraph of Section 13 confers upon the Federal Reserve Board the authority to prescribe limitations and restrictions on advances by Federal reserve banks to member banks on their collateral notes and that this authority is broad enough to empower the Board to prescribe seven days as a minimum

limitation for advances of this kind.

It may be regarded as questionable whether this proposed limitation on maturity of member banks' collateral notes is in harmony with the purpose of Congress in providing that Federal reserve banks may make advances to member banks on their promissory notes with maturities up to fifteen days. The following is a quotation from a letter addressed by the Governor of the Federal Reserve Board to Senator Owen in 1916 recommending the passage of this amendment:

> "The Board has recommended in the amendment designed to provide for 15-day loans, that member banks be permitted to put up as collateral paper of the kind they can now rediscount, or Government bonds in which they can now invest, and to obtain very short term loans based thereon. Experience has shown that in many cases where a bank would gladly obtain accommodation for a limited time, it does not care to go to the trouble of rediscounting paper for a specific period of maturity, although it would probably take advantage of an opportunity to obtain temporary accommodation if it could do so without having to borrow for the full period of the note's maturity, or otherwise comply with restrictions or limitations that may be deemed onerous. It is, therefore, recommended that the member banks be permitted to obtain of Federal reserve banks short period loans of this kind."

It seems apparent from this that it was contemplated that member banks might borrow on their promissory notes for very brief periods, even as short as one or two days.

As stated above, however, in my opinion the Board has the authority under the law to prescribe this limitation if it deems it advisable.

Respectfully,

(signed) George B. Vest,
Assistant Counsel.

(COPY)

X-6124-b

(Proposed new section of Regulation A to be inserted as Section X of Article A, subsequent sections to be renumbered accordingly.)

SECTION X. ADVANCES TO MEMBER BANKS ON THEIR PROMISSORY NOTES.

(a) Any Federal reserve bank may make advances to any of its member banks on their promissory notes provided such notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of the Federal Reserve Act or of the Regulations of the Federal Reserve Board, or are secured by the deposit or pledge of bonds or notes of the United States.

(b) No such advances shall be made for a period exceeding fifteen days nor for a period less than seven days. A note of a member bank given for any such advance in no case shall be cancelled or marked paid or shall be returned to the member bank until payment in full of both principal and interest thereof shall have been made not less than seven days after the advance to the member bank. No rebate of interest covering any part of such seven-day period shall be made in any case.

Ok
Pref. Rate.

#5

September 1, 1928.

Dear Governor Seay:

This will acknowledge receipt of your letter of August 30 with reference to the Board's recent published statement on preferential rates.

Your letter throws out a strong hint that you would like to know the locality of the clearing house, and confidentially, I have no objection in advising you that it was New Orleans.

With kind personal regards, I am,

Yours very truly,

R. A. Young,
Governor

Hon. George J. Seay, Governor,
Federal Reserve Bank,
Richmond, Virginia.

3321.3

FEDERAL RESERVE BANK
OF RICHMOND

August 30, 1928.

Dear Governor Young:

We today received two very interesting communications from the Board, one a statement for the press, reviewing and analyzing the credit situation, the other in reply to a communication from a clearing house association, proposing a preferential discount rate on member bank loans secured by government bonds.

It is difficult to believe that there is a clearing house in the United States worthy of the name which could make such a stultifying proposal. It would be very interesting indeed to know the locality of that clearing house. In these days, when government issues are apparently so heavily oversubscribed, no bank can take credit to itself for trying to assist the Government in placing its securities. I think the fact is sufficiently well understood that many of them are selfishly figuring on profit on government deposits as the outcome of such subscriptions. They deserve no consideration when caught by a decline in the market for such securities.

The Board's analysis of the credit situation is comprehensive and admirable and, at the same time, very temperate. It is a very timely communication to the public. I have never known such widespread misrepresentation of the credit situation by so-called reputable financial journals in different parts of the country. It is partly due to lack of understanding, and I believe it is partly due to selfish interest..

With kind regards, I am,

Very truly yours,

GJS-CCP

GEO. J. SEAY,
Governor.

Honorable R. A. Young, Governor,
Federal Reserve Board,
Washington, D. C.

New York Clearing House Assn

332.12

3323

August 29, 1928.

Gentlemen:

This will acknowledge receipt of your wire of August 27th to Governor Young recommending preferential discount rates by Federal reserve banks on collateral notes secured by Government obligations, the discount rate in each case to be the same as that borne by the security. Your proposal has been laid before the Federal Reserve Board, and, first, the Board feels justified in reminding you that the usual procedure under the law is for the Directors of the reserve banks to initiate rates. When such rates are initiated they are laid before the Board for review and determination. While the Board undoubtedly has the power to fix rates of discount for reserve banks we see nothing in the present situation to require such arbitrary action. At the same time the Board is not attempting to sidestep any responsibility it may have for reserve bank discount rates, and we advise your Association that if any reserve bank should initiate such preferential rates as you suggest the Board would be opposed to such procedure for the following reasons:

(1) It would not care to discriminate against commerce and industry by approving a rediscount rate of as low as three and one quarter percent on collateral notes secured by Government obligations while simultaneously certain reserve banks would be permitted to charge five percent on eligible commercial, agricultural and industrial paper.

(2) There is nothing in the present situation which would justify a lower rate on one class of Government securities over another. The previous action of the reserve banks that you refer to was a wartime measure only.

(3) If your proposal was put into effect at the present time it would permit a member bank to buy United States bonds in the present market on a yield higher than the bonds bear and the member bank would be prompted to rediscount to make such purchase solely for profit.

(4) Member banks own over four billions of United States Government bonds, and, upon reflection, we believe your Clearing House will agree with us that the invitation for profit would be too great for many of the banks to resist and only result in inflation that eventually would work widespread disaster to our entire financial

structure and, indirectly, to the business interests of the country.

(5) The proposed plan would have a strong tendency to appreciate the market value of the outstanding United States obligations bearing low rates and simultaneously depreciate those bearing higher rates, developing artificial and unwarranted prices for the various Government issues.

(6) Under normal peacetime conditions the Treasury Department should and does pay the ordinary market rates for money the same as any other borrowers. Moreover, the credit of the United States Government is so good that there is no occasion whatsoever of attempting by artificial means to place United States Government securities in a favored position as compared with commerce, industry and agriculture.

Very truly yours,

Secretary of the Treasury.
and Chairman of the Federal Reserve Board.

New Orleans Clearing House Association,

New Orleans, Louisiana.

X-6121

FEDERAL RESERVE BOARD

3323

S T A T E M E N T F O R T H E P R E S S

For release 3 o'clock p.m.
August 29, 1928.

There is quoted below a communication received by the Federal Reserve Board from a clearing house association:

"Referring to loans made member banks secured by United States securities we feel preferential rate of interest should be charged on transactions of this character, rate not to exceed rates borne by securities in accordance with previous ruling. In view of forthcoming financing by Treasury Department we feel this matter should receive the immediate and careful consideration of Federal Reserve Board. Present rates penalize banks assisting in financing."

The following is the Board's reply:

"Gentlemen:

This will acknowledge receipt of your wire of August 27th to Governor Young recommending preferential discount rates by Federal reserve banks on collateral notes secured by Government obligations, the discount rate in each case to be the same as that borne by the security. Your proposal has been laid before the Federal Reserve Board, and, first, the Board feels justified in reminding you that the usual procedure under the law is for the Directors of the reserve banks to initiate rates. When such rates are initiated they are laid before the Board for review and determination. While the Board undoubtedly has the power to fix rates of discount for reserve banks we see nothing in the present situation to require such arbitrary action. At the same time the Board is not attempting to sidestep any responsibility it may have for reserve bank discount rates, and we advise your Association that if any reserve bank should initiate such preferential rates as you suggest the Board would be opposed to such procedure for the following reasons:

(1) It would not care to discriminate against commerce and industry by approving a rediscount rate of as low as three and one quarter percent on collateral notes secured by Government obligations while simultaneously certain reserve banks would be permitted to charge five percent on eligible commercial, agricultural and industrial paper.

(2) There is nothing in the present situation which would justify a lower rate on one class of Government securities over another. The previous action of the reserve banks that you refer to was a wartime measure only.

(3) If your proposal was put into effect at the present time it would permit a member bank to buy United States bonds in the

present market on a yield higher than the bonds bear and the member bank would be prompted to rediscount to make such purchase solely for profit.

(4) Member banks own over four billions of United States Government bonds, and, upon reflection, we believe your Clearing House will agree with us that the invitation for profit would be too great for many of the banks to resist and only result in inflation that eventually would work widespread disaster to our entire financial structure and, indirectly, to the business interests of the country.

(5) The proposed plan would have a strong tendency to appreciate the market value of the outstanding United States obligations bearing low rates and simultaneously depreciate those bearing higher rates, developing artificial and unwarranted prices for the various Government issues.

(6) Under normal peacetime conditions the Treasury Department should and does pay the ordinary market rates for money the same as any other borrowers. Moreover, the credit of the United States Government is so good that there is no occasion whatsoever of attempting by artificial means to place United States Government securities in a favored position as compared with commerce, industry and agriculture.

Very truly yours,

(signed) A. W. Mellon,
Secretary of the Treasury and
Chairman of the Federal Reserve Board."

3823

Treasury Department

WESTERN UNION TELEGRAM

2—3786

Telegraph Office

RECEIVED
AUG 27 1928
OFFICE OF THE GOVERNOR

39W FN 109 40 EX

NEWORLEANS LA 840A AUG 27 1928

HON ROY A YOUNG GOVERNOR FEDERAL RESERVE BOARD

WASHN

"REFERRING TO LOANS MADE MEMBER BANKS SECURED BY UNITEDSTATES SECURITIES WE FEEL PREFERENTIAL RATE OF INTEREST SHOULD BE CHARGED ON TRANSACTIONS OF THIS CHARACTER RATE NOT TO EXCEED RATES BORNE BY SECURITIES IN ACCORDANCE WITH PREVIOUS RULING STOP IN VIEW OF FORTHCOMING FINANCING BY TREASURY DEPARTMENT WE FEEL THIS MATTER SHOULD RECEIVE THE IMMEDIATE AND CAREFUL CONSIDERATION OF FEDERAL RESERVE BOARD STOP PRESENT RATES PENALIZE BANKS ASSISTING IN FINANCING"

NEWORLEANS CLEARING HOUSE ASSOCIATION

J H PETERSON MANAGER AMERICAN BANK & TRUST CO CANAL BANK & TRUST CO HIBERNIA BANK & TRUST CO INTERSTATE TRUST & BANKING CO WHITNEY CENTRAL NATIONAL BANK WHITNEY CENTRAL TRUST & SAVINGS BANK

39W FN

WESTERN UNION TELEGRAM

2—3786

Treasury Department

#2

Telegraph Office

NEWORLEANS BANK & TRUST COMPANY MEMBERS OF

1015A

Reply Appd

AT BOARD MEETING

AUG 29 1928

Form No. 131.

Office Correspondence

FEDERAL RESERVE BOARD

Date May 29, 1928.

252

3323

332.3

2-8495 GPO

To General Counsel

From Mr. Eddy.

Subject:

At the meeting yesterday the Board voted to request you to prepare a draft of an amendment to the Board's regulations which would fix seven days as the minimum limitation on advances to member banks on their promissory notes secured by eligible paper or government securities.

It was also voted to refer this proposed regulation to the Board of Directors of the Federal Reserve Bank of New York for consideration and it is suggested that in submitting the amendment, you also submit a draft of a letter to the Chairman of the New York bank.

EXCERPT FROM MINUTES OF MEETING OF APRIL 27, 1928.

Mr. Miller then stated that he wished to submit for consideration another proposed motion on which he would not request immediate action, as follows:

> "That Counsel be instructed to prepare draft of an amendment to the Board's Regulations which would fix seven days as the minimum limitation on advances to member banks on their promissory notes secured by eligible paper or government securities."
>
> After discussion, Mr. Miller's proposed motion was laid on the table.

See Minutes
AT BOARD MEETING
MAY 28 1928

Re Bonds as Security

Gen. 422

3323
332.3

January 13, 1928.

Mr. W. M. Sherrill,
Caldwell & Company,
Union Street at 4th Avenue,
Nashville, Tennessee.

Dear Sir:

Receipt is acknowledged of your letter of January 10th in which you make inquiry as to a recent ruling of the Federal Reserve Board with regard to the types of bonds that are acceptable by the Federal reserve banks as collateral, other than government bonds.

If you have reference to the kinds of securities which may be used by member banks as collateral for advances made to them by Federal reserve banks on 15 day promissory notes, you are advised that the Federal Reserve Board has not made any recent rulings regarding the kinds of such collateral security. Under the Federal Reserve Act such notes of member banks must be secured by notes, drafts, bills of exchange or bankers' acceptances such as are eligible for rediscount or for purchase by Federal reserve banks, or by bonds or notes of the United States; bonds other than government bonds are accordingly ineligible as security for such notes.

It may be, however, that you have reference to the kinds of securities which may be deposited in the trust department of a national bank as security for funds of the trust department deposited in the commercial or savings department. The classes of securities which may be used for this purpose are described on pages 30 and 31 of the Regulations of the Federal Reserve Board, Series of 1928, a copy of which is enclosed herewith. There is also enclosed a copy of the regulations issued by the Comptroller of the Currency further defining the term "investment securities" as used in the Act approved February 25, 1927. You will note that these regulations of the Comptroller of the Currency are referred to on page 31 of the Board's Regulations.

In case the information given above does not answer the question which you have in mind, I will be glad to advise you further if you will state your inquiry more specifically.

Very truly yours,

(Signed) J. C. Noell

J. C. Noell,
Assistant Secretary.

15d.

GBV

Enclosures.

332.3

CALDWELL & COMPANY

BANKERS
INVESTMENT BONDS
UNION STREET AT FOURTH AVENUE
NASHVILLE, TENNESSEE

OFFICES IN
PRINCIPAL CITIES

January 10, 1928

Honorable J. C. Noel, Secretary,
Federal Reserve Bank,
Washington, D. C.

Dear sir:

The manager of our local Federal Reserve branch of the Atlanta bank has referred me to you for some information which we have been trying to secure for the past two or three months.

It is our understanding that there are now certain types of bonds that are acceptable by the Federal Reserve Bank as collateral, other than Government Bonds. This is undoubtedly covered under some recent ruling or new plan of the Federal Reserve Board. We will appreciate it very much indeed if you will supply us with the requirements of the Federal Reserve Bank with respect to bonds, other than Government Bonds, which may be used as collateral.

Some of our branch office managers have stated to us that other investment houses are pointing out to banks the advantage of making such substitutions, when they are acceptable to the Federal Reserve Bank.

Perhaps this information is covered in some recent circular issued by your Board which has not been received by our local branch of the Atlanta bank.

Thanking you very much for any information you may give us along the above lines,

Sincerely yours,

CALDWELL & COMPANY

WMS:IBA

BY: W. M. Sherrill.

FEDERAL RESERVE BANK

OF NEW YORK

January 22, 1924.

Dear Mr. Cunningham:

I am very glad to outline the procedure in our open market operations in connection with the so-called "repurchase transaction" and will endeavor to explain the relative importance of those transactions to the functioning of the open discount market as a whole and the relation of Federal reserve banks to that market.

Perhaps the best point of beginning would be a word regarding the open discount market as that term has come to be used in this country since the establishment of the Federal reserve banks and as it is understood in the financially important countries of Europe. In that sense the open discount market is the term applied to the transactions between banks, banking houses and investors in creating, buying and selling and carrying very liquid short dated securities, which are practically regarded as self-liquidating and from which the element of credit risk is regarded as practically eliminated.

Chief among such securities are bankers acceptances and short Treasury certificates, or Treasury bills as they are known abroad. Because of these qualities such securities are regarded in every important money center as suitable mediums for the employment of idle banking and other reserves, but even with all of these essential qualities they would still be unsuitable mediums for the employment of bank reserves unless their prompt convertibility into cash on occasion was also assured, and it is here that the central banks of Europe and the Federal reserve banks in this country render indispensable service to the discount markets of their relative countries. These markets are served by banking firms and other banking organizations which specialize in discount market operations. They are known variously as discount houses, discount dealers or brokers, although practically no brokerage business is done by any of the firms or corporations serving the New York discount market. In England, however, there is a distinct class which acts only as brokers.

These houses act as wholesalers and also retailers in the securities with which they deal; for instance, a bank or a corporation can always sell to one of these dealers, at a price, practically an unlimited amount of bankers acceptances or Treasury certificates. The dealer making the purchase ordinarily resells all or a substantial portion of them to other investing clients. These buyers may be local banks, corporations or individuals, or similar persons located in other parts of the country or abroad. The constant demand from such investors makes it necessary for the discount houses and dealers to carry at all times a large stock of paper assorted as to maturities, size of pieces, etc., required by the particular and diversified needs of their clients. As the gross profit of discount houses consists of but a very small fraction of 1% per annum, it is impracticable for them to carry their wares on their own capital. In fact, little of their own capital is employed and sufficient capital to conduct the business without borrowing could not be profitably employed as, because of the liquidity and strength of the instruments in which they deal, their yield is correspondingly low and so it is only by borrowing at correspondingly low rates of interest the money invested in their portfolios of bills and certificates that the business is possible.

Demand and short time loans to discount houses and dealers on the collateral of bankers and Treasury bills are preferred by many banks and bankers to their own investment in the securities and such loans constitute the great bulk of the call loans made by the banks of deposit in London. In this country the principal borrowers of call money are the Stock Exchange houses, who borrow against their holdings of investment securities but the difference in liquidity of a call loan made against bankers acceptances or Treasury bills and against the ordinary investment securities listed on the stock exchanges is that, in the event of the borrower having to realize on the collateral, he can do so at the Federal reserve bank or the Bank of England on short Government securities and bankers acceptances but he cannot do so on corporate stocks and bonds. To realize on them a purchaser must be found and that, in times of panic or stringency, often entails considerable loss and sometimes is almost impossible. This distinction is always recognized by banks of deposit

in London and in the large Continental centers, and by enough of them in New York to provide a moderate amount of low priced money to the discount houses.

Sometimes it is ample for their requirements but at other times sadly inadequate and it is at such times that the discount houses are permitted to sell their securities to Federal reserve banks, with an agreement to repurchase them within a few days. Generally the agreement to repurchase states fifteen days as the limit of time but they are always permitted to repurchase them sooner if they have occasion to do so; in fact, are expected to repurchase as soon as they can secure the necessary loan at an economic rate in the money markets.

A broad discount market is regarded in every country financially developed as an important national asset as through its operations the burden of financing international trade is spread over very wide areas. Idle funds available for short time employment are drawn from every section of the country and also, in normal times, from foreign countries, for investment in such a discount market. It is only through a discount market of this kind that bankers credit, as distinguished from bankers funds, can be put largely at the service of international trade, and the stabilizing effect of international credits upon the foreign exchanges of a country is well recognized.

In the United States the bankers acceptance credit and the discount market together permit the use of dollar credit in our overseas trade and relieve our importers and exporters from the hazards and fluctuations in the exchanges of foreign currencies, and also are of great benefit to the producer of agricultural products as they relieve the agricultural sections from the top heavy burden of local financing, or financing through borrowings, of crop movements. Once the cotton or grain is assembled in storage pending its orderly marketing and distribution into the channels of consumption, it serves as the basis for acceptance credit which is created by the strong, well known banks and accepting bankers, and their obligations are issued and sold in the open market, where they command the lowest rate of discount and give temporary employment to the funds from other sections of the country where funds are plentiful or even redundant, and also to funds of foreign countries. Thus,

while grain in Minnesota may be carried on the acceptance given by a bank in Chicago, the money that is invested in that acceptance and which is realized by the owner of the grain, may come from a bank or private investor in New York, San Francisco, Switzerland or Japan.

It is particularly interesting to observe how the center of credit strain shifts through a crop moving season. Taking Texas cotton as an example, we find during July and early August the Texas banks closely loaned up; then as the cotton begins to move, they liquidate very quickly but New England banks, which finance the New England cotton mills, begin to make money loans and give acceptance credits on account of the cotton which the New England mills have bought from the South, and presently we see in New York the bills created by New York banks against cotton exported to England and other countries in Europe, and the discount market, gathering money from every available quarter, provides the funds which really liquidate the loans of Texas banks.

The relation of Federal reserve banks to the discount market is primarily that of stabilizer, to relieve the market through purchase of an unwieldy temporary surplus of bills and to provide at all times that sense of security and confidence of ability to realize in the last analysis on discount market instruments which is essential to the maintenance of a discount market as a national asset. The opportunity for investment of reserve funds merely at the convenience of reserve banks is entirely secondary and inferior to this primary function.

In reply to your specific questions, the so-called repurchase transactions are conducted only with the firms and private corporations which specialize as discount houses and dealers who, by their great service to the market, have proven themselves worthy of our confidence and support in their undertaking. Being non-members, of course they have no rediscount facility, neither do they have deposits, and lacking these they could not adequately function in good weather and bad, as our money markets are now constituted, without this support from Federal reserve banks. The facility is never extended to member banks, which

are banks of deposit and also have the rediscount facility, but the benefits of it reach to member banks through the relief that it affords them when they have to withdraw loans which they have extended to the discount houses. We can see no abuses but only broad benefits to the country as the result of the development of this direct contact with the discount market. It is distinctly understood with all of the houses to whom we grant this facility, (and they are all houses of substantial capital and high standing who have made their financial statements and conditions thoroughly known to us), that they shall not come to us when money is procurable outside in sufficient volume at economic rates, and we have had no cases where this confidence has been abused. The machinery of the operation is very simple: the dealer to be accommodated, having executed and lodged with us a collateral agreement, addresses us in writing tendering the Government securities or eligible bankers acceptances that he desires to sell to us, reserving his right to repurchase them at a later date and contracting so to repurchase them. The transaction is generally arranged beforehand so that the receipt of the written contract and the relative securities is a simple matter. I am enclosing copy of the collateral agreement which we use and also copies of the form letters which constitute the sales contract.

Desirable as the practice is as an auxiliary to the functioning of the discount market, it should not, in our opinion, be extended to dealers in other classes of paper or securities; in fact, it could not be extended to promissory notes under the present law as they are ineligible for purchase and, aside from that, there exists no market for their resale. While promissory notes of well known borrowers are sold in the "commercial paper market" by the houses which are commonly referred to as note brokers, their function ceases when they have sold the paper to an investor and there is no resale market. That class of paper, therefore, is non-liquid as compared with Treasury certificates, bankers acceptances and prime trade acceptances which, having been bought for investment by a bank, may be again sold in the market.

I trust I have not burdened you with too long a letter on this subject but it is one that will stand a great deal of study and I have only touched a few of the high spots.

1/22/24.

It would give us a great deal of pleasure to have you come over to New York and spend some time with our officers who are familiar with every phase of the whole matter and go into it thoroughly with them, and I am sure they would be glad to arrange to have some of the prominent dealers and bankers from the discount market meet with you and discuss any of its problems that you would care to take up.

Very truly yours,

Pierre Jay,
Chairman.

Hon. E. H. Cunningham,
c/o Federal Reserve Board,
Washington, D. C.

Encs.

SALES CONTRACT

_____

Federal Reserve Bank of New York,

New York, N. Y.

Gentlemen:

We hand you herewith United States Government _____ _____, amounting to $_____par value, listed below, which we have to-day sold to you for the sum of $_____, and which we hereby agree to repurchase from you on or before _____, for the sum of $_____, and interest thereon at the rate of ____% per annum for the number of days that the said securities are held by you.

We are delivering as collateral security for the performance of this contract _____, of a par value of $_____, to be held by you subject to the terms and conditions of our general collateral agreement with you.

Very truly yours,

_____

_____

SCHEDULE OF SECURITIES OFFERED UNDER ABOVE SALES CONTRACT

Description of issue	Maturity	Amount (Par Value)

DATE_____

Federal Reserve Bank of New York,

New York City.

Gentlemen:

We have sent you this day, under separate cover, eligible bankers' acceptances to the amount of $_____, sold to you at _____% discount, which we hereby agree to repurchase at the same rate on or before_____with agreed right, to be exercised at our option, to repurchase these bills, either in whole or in part, prior to _____, to which date discount on today's sale has been calculated, as per detailed memorandum herewith.

We are delivering as collateral security for the performance of this contract, acceptance of (name)_____ (city)_____of a face value of $_____to be held by you subject to the terms and conditions of our general collateral agreement with you.

Yours very truly,

_____

KNOW ALL MEN BY THESE PRESENTS that in consideration of purchases and sales of bills, securities and/or other property effected between the Federal Reserve Bank of New York and the undersigned by virture of agreements from time to time entered into between the parties, it is hereby agreed that as collateral security for any and all liability of the undersigned to the said Federal Reserve Bank now or hereafter existing, matured or not matured, absolute or contingent, and whenever payable, including items held by said Federal Reserve Bank as security for any obligations of any sort whatever, said Federal Reserve Bank shall hold, retain and have a lien upon all moneys, negotiable instruments, bonds, stocks, commercial paper, credits, choses in action, claims and demands of every kind at any time in possession or control of said Federal Reserve Bank, or any of its agents or correspondents, or in transit to it by mail or carrier, belonging to, for account of, or subject to the order of the undersigned; and said Federal Reserve Bank shall have the following rights and powers in respect to such collaterals and every part thereof (in addition to any other rights which it may have): Said Federal Reserve Bank may at any time or times collect any of such collaterals, and it may indorse any thereof in behalf and in the name of the undersigned; and in case of failure of the undersigned to pay or discharge when due any such liability, or in case of failure of the undersigned to furnish additional collateral as hereinafter provided, or in case of the insolvency, general assignment, receivership, bankruptcy, or failure in business of the undersigned, said Federal Reserve Bank may sell without notice any of said collaterals at private or public sale, or at broker's board (being at liberty to become the purchaser if the sale is public or at broker's board) and may apply any and all money or credits, including the proceeds of any such sale, to the payment of expense of any such sale or sales, or of the realization or collection of any of said collaterals or of any of said liability of the undersigned, whether due or not due, and any and all liability of the undersigned shall in any of the cases above stated become due at the option of said Federal Reserve Bank, if the collateral securing liability of the undersigned to said Federal Reserve Bank shall at any time be unsatisfactory in amount or otherwise to said Federal Reserve Bank, or to any of its officers, the undersigned will immediately furnish such further security as will be satisfactory to said Federal Reserve Bank. Said Federal Reserve Bank may assign or transfer the whole or any part of any obligation or liability of the undersigned, and may transfer herewith as collateral

security therefor the whole or any part of the collateral above referred to, and the transferee shall have the same rights and powers with reference to the obligation or liability transferred and the collaterals transferred therewith, as are hereby given to said Federal Reserve Bank. It is also agreed that this instrument constitutes a continuing agreement between the undersigned and the said Federal Reserve Bank applying to all future, as well as existing, transactions between the said parties, and also that the force and effect hereof shall not be terminated by the closing at any time of all transactions between the said parties, but that the same shall apply thereafter to any new transactions and shall continue in full force until notice is received in writing by either party from the other of the intention to terminate it, whereupon, it shall be of no effect for any indebtedness subsequently created.

IN WITNESS WHEREOF

has caused these presents to be signed this

day of 192____

_____

By_____

STATE OF NEW YORK)
) ss.
COUNTY OF NEW YORK)

Before me, a Notary Public, in and for the County of , came to me known and known to me to be the person who executed the within agreement and who, being duly sworn by me, did depose and say that he is a partner of , and as such is duly authorized to execute the within agreement in behalf of said partnership, and that he so executed it for the uses and purposes therein expressed.

332.3

FEDERAL RESERVE BANK
OF NEW YORK

IN REPLY PLEASE REFER TO

January 29, 1924.

Dear Mr. Cunningham:

I have your letter 1/18/24 asking me for some information about repurchase agreements and their operation. It will give me great pleasure to send you a discussion of the subject early next week. The preparation of it has already been begun.

May I express my pleasure at your inquiry, and the hope that you will not hesitate at any time to write me asking me for any information you may desire on matters relating to this bank and this district.

Very truly yours,

Pierre Jay

Pierre Jay
Chairman.

Honorable Edward H. Cunningham,
Federal Reserve Board,
Washington, D. C.

PJ/RAH

332.3

January 18th, 1924.

Mr. Pierre Jay, Chairman,
Federal Reserve Bank of New York,
New York City.

Dear Sir:-

I am asking if you would be kind enough to give me, as near as you can, a picture of the actual proceedure followed in open market operations with respect to the so-called 're-purchase transaction'. I would also be pleased to have a copy of the option or agreement of re-purchase entered into. Are transactions of the above nature carried on with individuals and private corporations or are they confined to member banks? What, in your opinion, if any, are the abuses that tend to develop in the above practices? What, in your opinion, (providing the practice now is to deal with individuals and corporations) would prevent this privilege from being accorded to individuals and corporations dealing in other classes of eligible paper?

Dr. Miller has been very generous and patient with his explanations of the open market practices, but he has advised me to go to you at this time, as the one person who can give me the fullest information based upon actual proceedings. Hoping that you will feel free to give me any information that in your judgment will enable me to get the best picture in my mind of open market operations and re-purchase agreements possible, I am

Yours very truly,

E. H. Cunningham, Member,
Federal Reserve Board.

EHC.B.

November 28, 1923.

My dear Mr. Lever:

I have your letter of November 26th stating that it would greatly aid the financing of Federal and Joint Stock Land Banks, especially in the Fifth District, if the Federal Reserve Board could hold that the Federal Reserve Bank of Richmond "might accept the notes of member banks collateraled with the bonds of either of this type of institutions, somewhat on the same basis as are government bonds accepted as collateral." This question or something similar has several times been presented to the Board, and I read your letter to the Board this morning.

Notes of customers's of member banks collateraled by bonds of either the Federal Land Banks or the Joint Stock Land Banks may be accepted by the Federal Reserve Bank of Richmond, or by any other Federal reserve bank, provided that the proceeds of the notes have been used for a commercial or an agricultural purpose, but these bonds could not be used by member banks, themselves, as collateral for their 15-day notes, as can Government bonds which the member banks own. This is not, however, a matter of ruling by the Federal Reserve Board but is the law.

So far as customers' notes are concerned the collateral does not affect their eligibility, the question being the use of the proceeds except in the case of Government bonds. The law appears to provide that a man may borrow money for the purpose of buying Government bonds or for the purpose of carrying Government bonds which seems to be pretty broad and that a note given to a member bank may be rediscounted with the Federal Reserve Bank. This is contrary to the spirit of the Federal Reserve Act which is based upon the theory that notes given for business or agricultural purposes and self-liquidating through the sale of the goods or produce on which they were based are alone eligible for rediscount at a Federal reserve bank. It was, of course, not expected when the Federal Reserve Act was passed in 1913 that there would be any considerable number of Government bonds that could be purchased by individuals and used for collateral. The war changed that condition very seriously, and as you know the Reserve banks as well as the member banks were greatly hampered in 1920 by the fact that they were clogged up with bonds.

It certainly will not do to add to the number of bonds that can be used as collateral in the Federal Reserve System and it would be a good thing in all probability if we could so change the law that not even Government bonds could be used as collateral except on customers' notes, the proceeds of which had been used for a commercial purpose.

I may add that it doesn't seem to me that you are taking proper advantage of the tax exemption privilege on your bonds by selling them to local banks which are not large taxpayers. They ought to sell to better advantage among people who would obtain some advantage from the tax exempt privilege.

With best regards.

Yours very truly,

Hon. A. F. Lever,
Columbia, South Carolina.

P. S. - The very fact that local banks are willing to purchase tax free Joint Stock Land Bank bonds when they could presumably obtain plenty of good bonds yielding them a higher rate makes it apparent to me that the people who think that any considerable advantage can be obtained for the Treasury by curtailing the amount of tax free bonds are likely to find themselves mistaken. I think it will be shown that only a very small part of the tax free bonds are owned by the largest income taxpayers. Whatever the motive may be, they are held in small amounts by a vast number of people in institutions, nearly all of whom could invest in other bonds paying a sufficiently higher rate to cover taxes, or at least income taxes.

3323

THE FIRST CAROLINAS JOINT STOCK LAND BANK

MEMBER OF FEDERAL FARM LOAN SYSTEM
OPERATING IN NORTH AND SOUTH CAROLINA

A. F. LEVER,
PRESIDENT

COLUMBIA, S. C.

November 26th, 1923

Mr. Edmund H. Platt,
Member, Federal Reserve Board,
Washington, D. C.

My dear Mr. Platt:-

It would greatly aid the financing of Federal and Joint Stock Land Banks, especially in the Fifth District, if the Federal Reserve Board could hold that the Federal Reserve Bank at Richmond might accept the notes of member banks collateraled with the bonds of either of this type of institutions, somewhat on the same basis as are government bonds accepted as collateral. I don't know that the question has ever been presented to the Board, but a favorable ruling on this point would make it unnecessary, in a large measure, for these banks to go beyond their own immediate territorial limits to finance themselves and thus serve the purpose of the Farm Loan Act.

The South Carolina Tax Commission has just held that the bonds of the First Carolinas Joint Stock Land, for the purpose of taxation of capital shareholders' stock, is on a parity with government bonds and Federal Land Bank bonds of the Columbia bank. I enclose you a copy of the ruling. This ruling is aiding us greatly in the distribution of our bonds in the territory we serve, and if the Federal Reserve Board could bring itself to rule along the lines above suggested, it would greatly strengthen the position of these banks, and thus increase their usefulness in the service of the agriculture in their territory.

With personal regards and best wishes, I am

Yours very truly,

A. F. LEVER

President

AFL*RBW

Columbia, S. C., November 13, 1923.

Hon. A. F. Lever,
The First Carolinas Joint Stock Land Bank,
Columbia, S. C.

Dear Mr. Lever:-

The Tax Commission, after considering very carefully your request that the Commission rule that the bonds of the First Carolinas Joint Stock Land Bank, owned by South Carolina Banks, be put on the same basis for taxation as Liberty bonds and bonds of the Federal Land Bank of Columbia, is of the opinion that it was the purpose of the Legislature to encourage the banks of our state to invest in Federal Land Bank bonds with the view of helping agriculture through the farm loan system, and if this was the purpose of the Legislature, as we think it was, and as the Joint Stock Land Bank is doing the identical work of the Federal Land Bank of Columbia, we have endeavored to interpret Paragraph 30, Article 3, Section 342 of the code of laws of South Carolina by ruling that the tax exempt privileges of the Joint Stock Land Bank and the Federal Land Bank are identical.

Yours very truly,

SOUTH CAROLINA TAX COMMISSION.

By W. G. Query,

Chairman.

WGQ:JEH

C O P Y

Form No. 131.

Office Correspondence

FEDERAL RESERVE BOARD

232.3

Date Oct. 16, 1923.

To Mr. Cunningham

From Mr. Eddy

Subject: Purchase of Government Securities and bankers acceptances under re-purchase agreements.

2—8496

In accordance with the action of the Board at its meeting this afternoon, there is attached hereto copy of a letter from the Governor of the Federal Reserve Bank of Boston regarding the recent opinion of the Board's General Counsel as to the right of Federal Reserve Banks to buy Government securities and bankers acceptances, under re-purchase agreements.

(COPY)

FEDERAL RESERVE BANK

OF BOSTON

October 15, 1925.

Dear Governor Crissinger:

I enclose usual weekly report from our Havana agency, and am also enclosing extract from a personal letter received by one of our officers from Mr. Snow who is in charge of the agency.

I have read Mr. Wyatt's memorandum in which he expresses the opinion that Federal Reserve Banks have no power to buy Government securities and bankers' acceptances under repurchase agreements, and note that he advises the Board to issue a ruling that all such transactions be prohibited in the future. I sincerely hope that the Board will consider this question from every angle and that no definite action will be taken until after the conference next month.

Mr. Wyatt's opinion reverses opinions which have hitherto been given the Board by the Counsel's office. You may remember that when the Board authorized the Federal Reserve Bank of Atlanta to buy a large amount of Government bonds held by the Fourth and First National Bank of Nashville and to make a contract under which the Nashville bank obligated themselves to purchase and the Atlanta bank to resell, the whole question was discussed from two angles; first, as to the legality of the transaction, and second, as to the policy involved. While it was the consensus of opinion that the policy was bad, the Board nevertheless decided to allow the transaction to be made because of the emergency which confronted the Nashville bank. Agreement as drawn by the Atlanta bank was reviewed by the Board's counsel.

In reading Mr. Wyatt's brief I was struck by the fact that he was looking at the question from one angle alone. He did not seem to take into consideration the merits of a policy looking toward the maintenance of a broad market for Government securities and bankers' acceptances, and he ignored altogether the powers of Federal Reserve Banks as defined in Section 4 of the Act. Among the powers enumerated is the right to make contracts. I do not think that there is any question that subject to regulations of the Board, Federal Reserve Banks have the right to buy and sell bonds and notes of the United States in the open market, and that they also have the right to buy and sell bankers' acceptances and eligible bills of exchange. Having acquired such assets I do not see how there can be any question as to the right of a bank, under the powers given it in Section 4, to make a contract or agreement as to the disposition of these securities.

Our Counsel, Mr. Weed, agrees with me on this subject and at my request is preparing a brief which I shall be glad to send you when he has it ready.

If as a matter of policy, the Board should decide that no bills or Government securities should be bought under repurchase agreements I would suggest that the ruling be based entirely upon the Board's conception of a proper policy; but for the Board to take the position that such transactions are illegal would be to reverse its own position in the past and might have a serious effect upon the Atlanta Bank if the Fourth and First National Bank of Nashville should make good its threat to bring suit against that institution.

With all respect to Mr. Wyatt, I think that his opinion on this subject should be carefully reviewed before it is accepted.

Very truly yours,

(signed) W.P.G. Harding

W.P.G. Harding,
Governor.

Hon. D. R. Crissinger, Governor,
Federal Reserve Board,
Washington, D. C.

FEDERAL RESERVE BOARD

WASHINGTON

Confidential

X-3031
January 26, 1921.

Subject: Purchase of Certificates of Indebtedness from Borrowing Member Banks.

Dear Sir:

There is enclosed for your confidential information copy of a letter which was recently sent out by the Federal Reserve Bank of New York to 114 of its borrowing member banks.

It is estimated that exclusive of New York, eleven Federal Reserve Banks hold as collateral to member banks' fifteen day notes about $45,000,000 of Treasury Certificates of issues previous to that dated January 15, 1921. The Board believes that if you would care to point out to those of your member banks which are borrowing on Treasury Certificates that there is now a ready market for these issues, you could effect a substantial reduction in the volume of notes which you are carrying for member banks secured by Treasury Certificates.

As you know, the Board has been in communication with Federal Reserve Banks recently on the subject of rates of interest charged on paper secured by certificates. The Federal Reserve Banks of St. Louis and San Francisco have established a flat rate of 6% on all paper secured by these obligations without regard to the rate of interest borne by the certificates. There is enclosed for your further consideration copy of a memorandum received today from Assistant Secretary of the Treasury Gilbert, in which he points out the desirability of eliminating the present 5% and 5¼% rates.

In another communication, dated January 24th, Mr. Gilbert states that "Treasury certificates are now firmly established on an investment basis and it would be helpful to the general situation if borrowing banks generally would take steps to reduce their loans at the Federal Reserve Banks by further sales of Treasury certificates".

Very truly yours,

Governor.

TO GOVERNORS OF ALL F.R.BS. EXCEPT NEW YORK
COPIES TO CHAIRMEN " " "

Copy.

FEDERAL RESERVE BANK
NEW YORK

X-3031a
January 21, 1921.

Dear Sir:

You will be interested to know that the latest issue of U. S. Treasury certificates of indebtedness, which was dated January 15, 1921, has been more largely oversubscribed than any previous issue, thereby indicating the highly satisfactory condition of the certificate market. The allotments to this district of the January 15 certificates were about $138,000,000, while the subscriptions received at this bank totaled fully $300,000,000, which leaves an unsatisfied demand approaching $200,000,000 in this district alone.

With regard to the previous issues of Treasury certificates now outstanding, for which there is likewise a ready market, we find that a number of our member banks have pledged these certificates with us as collateral for advances and, although they are for the most part scattered among many banks in small amounts, the aggregate makes a sizeable figure. The unsatisfied demand in the market for certificates would readily absorb, on very favorable terms, the entire amount of certificates so pledged with us by member banks, and we are confident that we can sell all of the certificates which you own of the March 15, May 16 and June 15 maturities on a 5½% basis, and all of those maturing between August 16 and December 15 on a 5 5/8% basis.

As you know, it has been the desire of the Treasury to gradually get these certificates, as well as other Government securities, out of the banks and into the hands of investors, and we feel sure that you will agree with us as to the desirability of accomplishing this, especially with respect to such certificates as are used for loans at Federal Reserve Banks. The extent to which this has been accomplished is evidenced by the fact that there are at present $2,350,000,000 certificates of all issues outstanding, while the Federal Reserve Banks are now loaning only $131,000,000 or 5½% of that total against certificates. It is of obvious public advantage that borrowings at the Federal Reserve Banks should be gradually reduced in order to bring the System back to a normal basis, and one way to accomplish this result is to distribute certificates now held by the banks among ultimate investors.

We are bringing this matter to your attention as we believe it will be of interest to you to know that the present is an extremely favorable time to dispose of your holdings of certificates if you desire to do so.

We shall be glad to hear from you if we can be of any service in this connection.

Very truly yours,

(Signed) J. H. CASE,
Deputy Governor.

Copy

X-3031b

TREASURY DEPARTMENT

Washington

Assistant Secretary.

January 25, 1921.

TO GOVERNOR HARDING

The latest schedule of discount rates in effect at the several Federal Reserve Banks shows that at the Federal Reserve Banks of Philadelphia, Cleveland, Richmond, Atlanta, Chicago, Kansas City and Dallas, the discount rate on paper secured by Treasury certificates corresponds to the interest rate borne by the certificates, with a minimum of 5 per cent in case of Philadelphia, Atlanta, Kansas City and Dallas, and 5½ per cent in case of Cleveland, Richmond and Chicago. Entirely apart from the question of a flat 6 per cent rate on paper secured by Treasury certificates, it occurs to me that it would be desirable to clean up the situation by eliminating the rates under 5½ per cent, which are still possible under the present schedule at Philadelphia, Atlanta, Kansas City, and Dallas. There is only one issue of Treasury certificates now outstanding which bears interest at a rate lower than 5½ per cent, namely, the certificates of Series T M 1921, maturing March 15, 1921, which bear interest at 4¾ per cent. The amount of this series outstanding in the hands of the public is relatively small, namely, about $160,000,000, and the certificates can be readily sold in the market on about a 5½ per cent basis. Except for this one issue, the present 5 and 5¼ per cent rates in the banks named are, therefore, practically paper rates, which have fulfilled their purpose, and which, if continued, might invite a policy of offering Treasury certificates at too low a rate to be attractive as investments, in reliance on a level discount rate which would make it possible for the certificates to be pledged without loss at the Federal Reserve Banks. From this point of view particularly I think that the present 5 and 5¼ per cent rates should be eliminated, and that the present is a good time to accomplish it.

(Signed) S. P. Gilbert, Jr.

Form No. 231.

Office Correspondence

FEDERAL RESERVE BOARD

1245.1

Date August 9, 1920

To Federal Reserve Board

From Walter S. Logan

Subject: Right to prohibit use of member bank fifteen day notes secured by Government obligations as collateral for Federal reserve notes. 8495

3323

The opinion of this office has been asked as to whether there is any legal objection to the issuance of instructions by the Federal Reserve Board to Federal reserve agents that member bank fifteen-day collateral notes secured by United States bonds or notes are not to be accepted as collateral security for Federal reserve notes.

The following provisions of Section 16 of the Federal Reserve Act should be considered in connection with this question:

"Federal reserve notes, to be issued at the discretion of the Federal Reserve Board for the purpose of making advances to Federal reserve banks through the Federal reserve agents as hereinafter set forth and for no other purpose, are hereby authorized." * * * * * *

"Any Federal reserve bank may make application to the local Federal reserve agent for such amount of the Federal reserve notes hereinbefore provided for as it may require. Such application shall be accompanied with a tender to the local Federal reserve agent of collateral in amount equal to the sum of the Federal reserve notes thus applied for and issued pursuant to such application. The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances acquired under the provisions of section thirteen of this act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of section fourteen of this act, or bankers' acceptances purchased under the provisions of said section fourteen, or gold or gold certificates; but in no event shall such collateral security, whether gold, gold certificates, or eligible paper, be less than the amount of Federal reserve notes applied for". * * * * * *

"The Board shall have the right, acting through the Federal reserve agent, to grant in whole or in part, or to reject entirely, the application of any Federal reserve bank for Federal reserve notes". * * * * * *

"Any Federal reserve bank may at its discretion withdraw collateral deposited with the local Federal reserve agent for the protection of its Federal reserve notes issued to it and shall at the same time substitute therefor other collateral of equal amount with the approval of the Federal reserve agent under regulations to be prescribed by the Federal Reserve Board". * * * * * *

It is to be noted that under these provisions the issuance of Federal reserve notes is subject to the discretion of the Federal Reserve Board and that the right is expressly given to the Board to grant in whole or in part, or to reject entirely, any application for Federal reserve notes. Also, in the case of the substitution of collateral the substitution is to be made "with the approval of the Federal Reserve Agent under regulations to be prescribed by the Federal Reserve Board.

In view of these provisions of Section 16, I am clearly of the opinion that the Federal Reserve Board has authority to instruct Federal Reserve Agents to reject any application for Federal reserve notes if the collateral security tendered with such application consists of member bank fifteen-day collateral notes secured by bonds or notes of the United States.

Respectfully,

Walter S. Logan

WSL-B

General Counsel.

7/3/20 Strictly Confidential

X-1972

MEMBER BANKS COLLATERAL NOTES
SECURED BY COVERNMENT WAR OBLIGATIONS.

~~332.3~~
332.3

The Act approved September 7, 1916, amended Section 13 of the Federal Reserve Act by adding thereto the following paragraph: 7/3/20

Carded

"Any Federal Reserve Bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal Reserve Bank, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act or by the deposit or pledge of bonds or notes of the United States."

This particular amendment was suggested to the Banking and Currency Committees of the House and Senate by the Federal Reserve Board in the Spring of 1916, at a time when little use had been made of the rediscount facilities of the Federal Reserve Banks. Experience had shown that quite a number of the larger member banks could use funds to advantage for a few days at a time and would be willing to secure accommodations from the Federal Reserve Banks for short periods, while they would have no occasion to use the funds for thirty, sixty or ninety day periods, and the banks as a rule were reluctant to offer for discount paper the maturity of which ran longer than the time for which funds were needed. It frequently happenad

Indexed copy filed 332.3-1

that banks having occasion to use funds for a few days only would not have available paper of very short maturity in sufficient volume to satisfy their requirements and in order that the Federal Reserve Banks might be in position to respond to the short time needs of member banks the Board suggested the foregoing amendment.

Before Congress had taken action, however, and as the summer advanced, it became more and more evident that the United States might be drawn into the World War, and in order to be in a position to facilitate Government financing in such an event the Board suggested that member banks' fifteen day collateral notes might be secured also by the deposit or pledge of bonds or notes of the United States. Up to May, 1917, member banks' collateral notes discounted by Federal Reserve Banks were secured almost entirely by "notes, drafts, bills of exchange or bankers' acceptances eligible for rediscount or purchase", but since the issue of the first series of Treasury Certificates of Indebtedness and of the first Liberty Loan, member banks' collateral notes have been secured almost entirely by bonds and notes of the United States.

It seems, therefore, that it would be proper to divide member banks' fifteen day collateral notes into two classes; (1), those secured by "notes, drafts, bills of exchange or bankers' accept-

ances eligible for rediscount or purchase", and (2), those secured by "bonds and notes of the United States". With respect to the first class, it is evident that such notes are offered by member banks for the purpose of securing short time accommodations for the exact time the funds are needed. Where credit is required for a longer time a member bank would endorse the "notes, drafts, bills of exchange or bankers' acceptances" and rediscount them with the Federal Reserve Bank. Transactions of this kind do not call for any concession in rate and such notes should properly take the rate established for rediscounts of longer maturities.

As to class (2), however, the situation is different. Member banks have always been the purchasers and distributors of Treasury Certificates and they were to a very large extent the purchasers and distributors of the various issues of the Government's war bonds. Pending distribution it was necessary for most of the member banks, and particularly those which subscribed for liberal amounts, to borrow from the Federal Reserve Banks and the fifteen day collateral notes secured by Treasury Certificates, Liberty Bonds and Victory Notes have always been used as a means of getting the needed accommodations from the Federal Reserve Banks.

Paragraph (d) of Section 14 authorizes the Federal Reserve Banks, subject to the review and determination of the Federal Reserve Board to establish rates of discount "for each class of

paper" and while the banks may classify paper according to maturity or according to the character of security, they cannot draw any distinction between notes secured by the same class of collateral. Thus a Federal Reserve Bank may establish one rate of discount for member banks' collateral notes secured by commercial paper eligible for discount and another rate of discount on notes secured by bonds and notes of the United States, but it cannot establish two distinct rates of discount on notes secured by notes and bonds of the United States.

Therefore while the purpose of Congress in permitting notes or bonds of the United States to be used as collateral to members banks' fifteen day notes was to facilitate the war financing of the Government, no consideration can be given in establishing discount rates for such paper to the circumstances attached to the ownership of notes and bonds of the United States by borrowing banks. It follows, therefore, that if a preferential rate of discount should be established for notes of class (2), member banks could avail themselves of the opportunity thus afforded of securing commercial accommodations at the lower rate, and an incentive would be given to the borrowing of bonds by member banks and there would be danger of an undue expansion of credit.

But while a Federal Reserve Bank cannot establish differential rates on paper of a given maturity having the

same security, it is not prohibited by law from adopting the policy of receiving certain notes for discount and declining to consider application for discount of other notes. Therefore it would seem in the present circumstances that a Federal Reserve Bank might properlydivide member banks' collateral notes into two classes as outlined above, and discount class (1), that is, notes secured by eligible commercial paper, at the current market rates for thirty day paper, and decline to receive for discount notes of class (2), that is, notes secured by bonds and notes of the United States, unless the bonds and notes of the United States are actually owned by the borrowing bank and are directly connected with the war financing of the Government. As Treasury certificates are being issued to take care of the floating obligations of the Government arising out of the war, and as the purchase of these certificates by the banks is an accommodation to the Government, member banks' promissory notes secured by such certificates, having not longer than fifteen days to run, should be taken freely and there can be no objection to a preferential rate on paper of this class. The Board's policy has been to approve the same rate on paper secured by Certificates of Indebtedness as the certificates themselves bear.

This leaves to be considered member banks' promissory notes

secured by the various issues of Liberty Bonds and Victory Notes. The Board has never approved any preferential rate on member banks' collateral notes which were secured by bonded obligations of the United States other than bonds issued since April, 1917, but has taken the position consistently that the preferential rates given to notes of this class are for the accommodation of the Government in its war financing. In some districts there are many member banks which for patriotic reasons subscribed heavily to the Government war bond issues and some of them have not liquidated their holdings of such bonds to an extent which would relieve them of the necessity of borrowing from the Federal Reserve Banks on them. There are cases also where member banks have liquidated entirely their original subscriptions to Government bonds and have repurchased bonds for the sake of investment at the lower rates now prevailing in the market, or where member banks have borrowed bonds from their customers and have used them as collateral to fifteen day notes for the purpose of obtaining funds with which to make commercial loans.

There does not seem to be any reason why a Federal Reserve Bank should receive for discount member banks' collateral notes which are secured by borrowed bonds or bonds bought purely for investment, and the inquiry is therefore made whether your Federal Reserve Bank would care to adopt the policy of declining to discount for member

banks their fifteen day collateral notes when secured in this manner and announce that hereafter it will be its policy to confine such transactions only to offerings of notes which are secured by Liberty Bonds and Victory Notes, actually subscribed for in good faith by the borrowing bank before the allotment of the final issue of Government war bonds, that is, the Victory Notes.

The Federal Reserve Banks should also require that all collateral pledged as security to member banks' fifteen day notes have a market value at least equal to the face of the note. Therefore in discounting member banks' collateral notes secured by Liberty Bonds and Victory Notes actually subscribed for and owned by the member bank, a Federal Reserve Bank should require, first, that such notes be secured by an amount of such bonds, the face value of which is equal to the amount of the note, and s second, that the deficiency between the market value of such bonds and the face of the note be covered by the pledge of additional notes or bonds of the United States, or by the pledge of notes, drafts, bills of exchange or bankers acceptances eligible for discount or purchase by the Federal Reserve Banks.

In consideration of all the attendant circumstances and in further consideration of the fact that by the limitations above outlined, it is clear that under this plan there can be no use of Government war obligations as

collateral to member banks' fifteen day notes for the purpose of securing commercial accommodations at reduced rates, and therefore no additional inflation or expansion of credit, it would be proper for a Federal Reserve Bank to bear in mind the circumstances under which the bonds pledged with it are acquired and to make a liberal concession in the discount rate on such paper, that is, on member banks' fifteen day promissory notes secured by Liberty Bonds and Victory Notes actually subscribed for and acquired from the Government by the borrowing bank, or taken before the final allotment of Victory Notes, from borrowing subscribers in default. In the Board's opinion, however, it would not be wise to make the rate on paper of this classification uniform with the rate borne by the bonds, for there should be no incentive to the borrowing banks to hold bonds as a basis of collateral to loans indefinitely. It has been suggested that where the notes are secured by Victory Notes which bear 4-3/4% interest that the rate of discount be 5% and where notes are secured by Liberty Bonds bearing 4-1/4% interest that the rate of discount be 4-1/2%. It is further suggested that a Federal Reserve Bank, if it should adopt the foregoing policy and schedule of rates, should inform its member banks that they will be expected in view of the favorable rate accorded them to make a reasonable reduction in the amount of such notes at the end of each fifteen day period. The member banks could well afford to make this reduction equal at least to the amount of interest saved.

X 1972

It is clearly impracticable to give any preferential rate to customers' notes which are secured by Liberty Bonds. This would open up avenues for too large an extension of credit when the large volume of Liberty Bonds outstanding is considered. A Federal Reserve Bank, therefore, should continue to discount for member banks customers' notes secured by Liberty Bonds and Victory Notes at the established commercial rate. Such customers' notes, however, ought not to be used as collateral to member banks' fifteenday notes of class (2).

July 3, 1920.

Copy filed 332.3-1

July

Mar 6 1930

Form 148

TELEGRAM

FEDERAL RESERVE BOARD

LEASED WIRE SERVICE

WASHINGTON

TRANS 5

June 18, 1920.

Curtiss, Boston	Hardy, Richmond	Rich, Minneapolis
Jay, New York	McCord, Atlanta	Ramsay, Kansas City
Austin, Philadelphia	Heath, Chicago,	Ramsey, Dallas
Wills, Cleveland	Martin, St. Louis	Perrin, San Francisco

Please wire Board early as practicable tomorrow June 19 total number of member banks borrowing from Federal Reserve Bank, either on their own collateral notes or through rediscount of eligible paper, as at close of business today.

EMERSON.

FEDERAL RESERVE BOARD

WASHINGTON

332.3

June 15, 1920.

X-1954

Canceled

Subject: Value of Security for Collateral Notes Rediscounted.

Dear Sir:-

The Governor of a Federal Reserve Bank has advised the Board that his Bank has discounted for another Federal Reserve Bank several million dollars worth of collateral notes and that figuring the value of the collateral at the present market price, there is an average deficiency in the collateral of about 6.7 percent. He states that these notes and collateral are held for the account of the Federal Reserve Agent of his Bank and that Federal Reserve notes are issued against them for the full amount of the notes. He asks whether in these circumstances his Bank should accept collateral from other Federal Reserve Banks at more than the market price.

The Board has considered this question and desires that all Federal Reserve Banks be informed that they are expected in their discount transactions for other Federal Reserve Banks to require that all collateral notes discounted be fully secured, that is, that the market price of the collateral be equal to the face of the notes. The Board would suggest, however, that Federal Reserve Banks which hold collateral notes discounted for other Federal Reserve Banks give the borrowing banks a reasonable time, say until July 1st, to make good any deficiency in collateral.

Very truly yours,

Governor.

FEDERAL RESERVE BOARD

WASHINGTON

January 26, 1920.

X-1810

Stamped

Subject: Preferential Rates of Discount on Member Bank Notes.

Dear Sir:

With further reference to the Board's wire of January 22 with regard to the ruling of the Board's Counsel on the subject "Preferential rates of discount on member bank notes", there is enclosed herewith for your information the full text of the opinion.

Very truly yours,

Governor.

Letter to Governors - copy to Chairman.

Enclosure. X-1809

Original copy filed 332.3-9

FEDERAL RESERVE BOARD X-1809
WASHINGTON

January 20, 1920

Memorandum for
Governor Harding

Subject: Preferential rates of discount on member bank notes.

Dear Governor Harding:

You have asked the following question:- If the Federal Reserve Board approves a Federal Reserve Bank's recommendation of preferential rates of discount for member bank notes secured by certificates of indebtedness of the United States, or by Liberty Bonds or Victory Notes, may the Federal Reserve Bank make advances at those rates only when the certificates of indebtedness, bonds or notes pledged as security are actually owned by the member bank procuring the advance and only when the Government deposit of such bank, if any, at the time that the advance is made is also secured respectively by certificates of indebtedness, Liberty Bonds or Victory Notes actually owned by the bank.

There is no doubt that a Federal Reserve Bank may establish and the Federal Reserve Board may approve preferential rates of discount upon member bank notes secured by certificates of indebtedness, Liberty Bonds or Victory Notes; that has already been done in previous instances. There is also no doubt that the exercise of the power conferred upon a Federal Reserve Bank to make advances upon member bank notes secured by certificates of indebtedness, Liberty Bonds or Victory Notes, is purely optional with the Federal Reserve Bank and not mandatory. The Federal Reserve Board has frequently had occasion to rule that the word "may" as used in the Federal Reserve Act in contradistinction to the word "shall" is permissive, and that powers conferred upon reserve banks by that word, may or may not be exercised in the discretion of the Board of directors of the Federal Reserve Bank. In the exercise of that discretion, however, the board of directors is required by the terms of Section 4 of the Federal Reserve Act to -

> "administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and shall, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks."

From a legal standpoint, therefore, it is clear that if a Federal Reserve Bank establishes and the Federal Reserve Board approves preferential rates upon member bank notes secured by certificates of indebtedness, Liberty Bonds or Victory Notes, the reserve bank may, as a matter of administration, refuse to make an advance on such notes unless the certificates of indebtedness, bonds or notes pledged as security are actually owned by the member bank and unless the Government deposit of such bank, if any, at the time such advance is made is also secured respectively by certificates of indebtedness, Liberty Bonds or Victory Notes actually owned by it.

The Federal Reserve Board in transmitting its approval of a rate may, of course, advise the reserve bank of the nature of its powers referred to above. An expression of the Board's opinion in that respect may be helpful to the reserve bank in the effective administration of its preferential rates.

Respectfully,

GEORGE L. HARRISON.

General Counsel.

This letter sent to the Federal Reserve Agent of each bank except St. Louis.

332.3 Gen.

December 19, 1919.

All Banks

Mr. Frederic H. Curtiss,
Federal Reserve Agent,
Boston, Mass.

Dear Sir:

Will you be so good as to send to the undersigned a copy of the form of collateral note used by your bank in making 15-day advances to member banks?

Very truly yours,

(Signed) W. W. Hoxton

Executive Secretary.

Mr. Francis Hoxton 6/17/20

FEDERAL RESERVE BOARD
WASHINGTON

The telegram given below is hereby confirmed. ----------
Assistant Secretary.

2—7729

December 4, 1919. 332.3

Curtiss,	Boston,	Hardy,	Richmond	Rich,	Minneapolis,
Jay,	New York,	McCord,	Atlanta,	Ramsay,	Kansas City,
Austin,	Philadelphia,	Heath,	Chicago,	Ramsey,	Dallas,
Wills,	Cleveland,	Martin,	St. Louis,	Perrin,	San Francisco.

Beginning with report of condition of member banks as of December fifth please segregate items 14 and 15 form St. 51 member banks' collateral notes also bills discounted for member banks as follows: Member banks' collateral notes secured by United States war obligations and war paper code HERR for Federal Reserve bank cities, code KORB for Federal Reserve branch cities, code PARK for all selected cities. Member banks' collateral notes otherwise secured, codes HOOF, KALB, PRAG respectively. Bills discounted for member banks secured by U.S. war obligations and war paper, codes HUTE, KNOB, PEON. Bills discounted for member banks, all other, codes HUSS, KARS, PLOW respectively.

HARDING.

FEDERAL RESERVE BOARD

WASHINGTON

August 12, 1918.

X-1120

Dear Sir:

There is inclosed for your information copy of an opinion by Counsel as to the treatment as a liability of the maker to the bank for borrowed money, of a note which has been rediscounted by a member bank. The Board does not mean to suggest that member banks should avail themselves generally by rediscounting, of their authority to grant lines of credit in excess of 10 per cent of their capital and surplus as prescribed by Section 5200 of the Revised Statutes, as it is the belief of the Board that wherever compatible with the public interest, credit should be curtailed rather than expanded. Banks should keep in mind their contingent liability on rediscounted paper which, if not paid by the maker, must be taken up by the endorsing bank, and if unable to rediscount a renewal, the bank would find itself encumbered with an excess line. In cases, however, where banks wish to grant larger credits with Government obligations as security, the power outlined in the Counsel's letter may be availed of to advantage.

Very truly yours,

Governor.

The Governor,
Federal Reserve Bank,

Inclosure.

Index Copy filed 332.2-41

COPY

X-1120a

FEDERAL RESERVE BOARD

WASHINGTON

August 7, 1918.

M. C. Elliott
Counsel

My dear Governor:

In an opinion approved by the Board and published on page 638 of the July, 1918, Bulletin, the question was considered whether a note rediscounted by a member bank should thereafter be treated as a liability of the maker to the bank for borrowed money. In that opinion the following statement appears:

> "This question was considered by the Board and by the office of the Comptroller in connection with the limitations prescribed by Section 5200 Revised Statutes on liabilities to a national bank of any one person, firm or corporation.
>
> The conclusion was reached in that case that notes which have been rediscounted by a national bank and which are no longer owned or held by the bank, should not be included as a liability of the maker to the bank for borrowed money within the meaning of Section 5200."

Exception has been taken to this conclusion by some of the officers of the Federal reserve banks, and by certain national bank examiners, and there seems to be some apprehension on their part that this ruling of the Board may be used by member banks for the purpose of evading the limitations prescribed by Section 5200.

You have asked this office to give further consideration to the question involved and to suggest what, if any, action the Board or the Comptroller should take to prevent excessive loans from being made under authority of this ruling.

THis question is one which involves the application of the law of negotiable instruments.

Under Section 5136 Revised Statutes, which prescribes the corporate powers of national banks, such banks are authorized, among other things, to discount and "negotiate" promissory notes.

Under the Negotiable Instruments Law (Sec.30) "An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof".

Under Section 5200 Revised Statutes the liabilities to a national bank of any one person for borrowed money are limited to an amount which must not exceed ten per cent of the capital and surplus of the lending bank.

Under authority of these two sections it is clear that a national bank may discount the note of a customer which does not exceed in amount ten per cent of its capital and surplus and may subsequently negotiate or sell this note to a bona fide purchaser for value without notice.

The question involved is whether the maker of the note continues liable to the bank after the note has been negotiated and is owned by a bona fide holder in due course.

Section 51 of the Negotiable Instruments Law provides that -

> "The holder of a negotiable instrument may sue thereon in his own name and payment to him in due course discharges the debt".

It is clear, therefore, that when such a note is rediscounted by a bank its rights are transferred to the holder in due course and the maker becomes liable to the holder. It necessarily follows that the maker's liability to the bank ceases. If this were not true the maker might obtain a discharge of his liability on the note by paying the bank even after it had transferred its rights by endorsement of the note to a bona fide holder.

To hold that the maker of a note continues liable to a national bank for money borrowed, after the bank has rediscounted the note, would be equivalent to holding that a negotiable promissory note loses its negotiability when discounted for the maker by a national bank. There is clearly no legal justification for such a conclusion.

It has been suggested that the position taken in the opinion under consideration constitutes a radical departure from previous rulings of the Comptrollers office.

It is true that for many years it was customary for national banks to continue to carry as assets notes which had been rediscounted. This practice, which necessarily resulted in a duplication of the assets of national banks, has, however, been discontinued and while the reports of condition now show the amount of bills or notes rediscounted these amounts are not included in the total assets of the bank.

It necessarily follows that unless a note remains an asset of a bank after it has been rediscounted it does not constitute a liability of the maker to the bank but becomes a liability of the maker to the bona fide holder.

This principle has been consistently recognized by the Comptroller's office in the administration of the estates of failed banks. The maker of a note held by a failed bank is ordinarily entitled to offset his deposit balance with the bank against the note but in the administration of receiverships the Comptroller has consistently declined to allow the maker of a note to offset his deposit balance if the note is not in the hands of the receiver but is held by some other bank under rediscount on the ground that he may thereby obtain preference over other creditors to the extent of the offset if the estate of the bank is insufficient to pay the depositors in full. This question was involved in the case of United States Bank v. McNair, 116 N. C. 550; 21 S. E. 389. In that case the maker of the note was endeavoring to have his liability treated as a liability to the bank in order to obtain the benefit of an offset but the court disallowed his claim.

With all due deference to the opinion of those who have taken exception to this ruling of the Board, the fear that it may be successfully used by banks to evade the limitations of Section 5200 seems to be very much exaggerated.

So long as the customer's paper is well secured or is of such intrinsic value as to find a ready market with other banks the contingent liability incurred by the endorsing bank is not of serious consequence. On the other hand, if the paper offered for rediscount is not intrinsically valuable and the offering bank is merely seeking to evade the limitations of Section 5200, it is not likely that other banks would feel disposed to rediscount such paper. They would in such case be much more likely to require the borrowing bank to execute its note secured by its customer's note with a proper margin, in which case the customer's paper would remain the property of the borrowing bank and would have to be included in the liabilities of the makers to the borrowing bank. If the borrowing bank, in order to evade the limitations of Section 5200, should enter into an agreement with its correspondent to repurchase rediscounted paper before maturity, or to leave the proceeds of the rediscount on deposit with it, the transaction would not have been entered into in good faith and an examiner or officers of a Federal reserve bank would be justified in treating such paper as subject to the limitations of Section 5200.

As stated by Daniel on Negotiable Instruments (Section 779-b, Volume 1, Sixth Edition)-

"Under several provisions of the statute (Negotiable Instruments Law), it is held that merely giving the transferrer credit does not constitute the transferee a holder in due course. Thus when a bank simply discounts a note and credits the amount thereof on the endorser's account, without paying to him any value for it, such bank is not a purchaser for value or a holder in due course as defined by the statute". (Albany County Bank v. People's Co-operative Ice Co., 86 N. Y. S. 772, 92).

If, however, a bank negotiates a note of its customer in good faith in order to obtain additional funds to take care of the needs of other customers, there would seem to be no justification for treating the liability of its customer to the bona fide holder of the note as a liability to the bank itself. The fact that the bank is contingently liable as endorser and may be called upon to pay the note if the maker defaults should very properly be taken into consideration in determining liabilities that may be incurred by the bank under Section 5202 but should not be taken into consideration in determining the liabilities that may be incurred to the bank under Section 5200.

The Board has heretofore ruled that a national bank may lend to one customer an amount equal to ten per cent of its capital and surplus and may thereafter accept drafts of the same customer under authority of the Federal Reserve Act. In this case the bank assumes a direct and not a contingent liability on the drafts accepted and is the primary obligor. This fact, however, does not justify the Board in requiring banks to treat this liability assumed by the bank as a liability of its customer to the bank for borrowed money within the meaning of Section 5200.

If the Board feels that it is necessary to take any affirmative action to prevent its ruling from being used by member banks as a means of evading the limitations of Section 5200, it is suggested that it might amend Section III of Regulation "A", series of 1917, to read substantially as follows:

III. Applications for Rediscount.

"All applications for the rediscount of notes, drafts or bills of exchange, must contain

a certificate of the member bank in form to be prescribed by the Federal reserve bank, that to the best of the knowledge and belief of the officers of the applicant bank, such notes, drafts or bills of exchange have been issued for one or more of the purposes mentioned in 2 (a); such certificate shall also show whether the notes, drafts or bills discounted for any one borrower whose paper is offered for rediscount, exceeds ten per cent of the capital and surplus of the applicant bank, including notes, drafts or bills held in its own portfolio or under rediscount with other banks.

If the aggregate of such notes, drafts or bills does exceed ten per cent of the capital and surplus of the applicant bank, such certificate shall show (a) the amount held in its own portfolio, (b) the amount rediscounted with other banks, (c) the amount and character of security held, (d) whether or not the member bank is under agreement to repurchase at or before maturity notes, drafts and bills rediscounted, (e) whether or not it has received the actual proceeds of notes, drafts and bills rediscounted or merely a book credit therefor."

With this regulation in force, the Federal reserve bank would be able to determine the amount of secured and unsecured paper discounted by the applicant bank for any one borrower and rediscounted with other banks. If properly secured, the contingent liability of the member bank on the paper rediscounted in good faith would constitute merely a nominal liability. On the other hand, if the intrinsic value of the paper rediscounted appeared to be such as to make it more than probable that the endorsing member bank would be called upon to pay it, the Federal reserve bank could in its discretion determine whether such paper though technically eligible should be accepted for rediscount by the Federal reserve bank.

The Comptroller of the Currency might in like manner require national banks to show in their reports of condition information called for in the Regulation of the Board as amended in accordance with the foregoing suggestion.

The National Bank Examiner might likewise require the officers of the national bank to certify on oath whether the bank is under agreement to repurchase rediscounted paper and whether it has received the proceeds of such paper or merely a book credit and, for reasons hereinbefore stated, might treat all paper rediscounted under an agreement to repurchase or for which merely book credits have been received, as subject to the limitations of Section 5200.

Respectfully,

M. C. Elliott,

Counsel.

Hon. W. P. G. Harding,
Governor,
Federal Reserve Board.

COPY

X-1120a

FEDERAL RESERVE BOARD

WASHINGTON

August 7, 1918.

M. C. Elliott
Counsel

My dear Governor:

In an opinion approved by the Board and published on page 638 of the July, 1918, Bulletin, the question was considered whether a note rediscounted by a member bank should thereafter be treated as a liability of the maker to the bank for borrowed money. In that opinion the following statement appears:

> "This question was considered by the Board and by the office of the Comptroller in connection with the limitations prescribed by Section 5200 Revised Statutes on liabilities to a national bank of any one person, firm or corporation.
>
> The conclusion was reached in that case that notes which have been rediscounted by a national bank and which are no longer owned or held by the bank, should not be included as a liability of the maker to the bank for borrowed money within the meaning of Section 5200."

Exception has been taken to this conclusion by some of the officers of the Federal reserve banks, and by certain national bank examiners, and there seems to be some apprehension on their part that this ruling of the Board may be used by member banks for the purpose of evading the limitations prescribed by Section 5200.

You have asked this office to give further consideration to the question involved and to suggest what, if any, action the Board or the Comptroller should take to prevent excessive loans from being made under authority of this ruling.

THis question is one which involves the application of the law of negotiable instruments.

Under Section 5136 Revised Statutes, which prescribes the corporate powers of national banks, such banks are authorized, among other things, to discount and"negotiate" promissory notes.

Under the Negotiable Instruments Law (Sec.30) "An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof".

Under Section 5200 Revised Statutes the liabilities to a national bank of any one person for borrowed money are limited to an amount which must not exceed ten per cent of the capital and surplus of the lending bank.

Under authority of these two sections it is clear that a national bank may discount the note of a customer which does not exceed in amount ten per cent of its capital and surplus and may subsequently negotiate or sell this note to a bona fide purchaser for value without notice.

The question involved is whether the maker of the note continues liable to the bank after the note has been negotiated and is owned by a bona fide holder in due course.

Section 51 of the Negotiable Instruments Law provides that -

> "The holder of a negotiable instrument may sue thereon in his own name and payment to him in due course discharges the debt".

It is clear, therefore, that when such a note is rediscounted by a bank its rights are transferred to the holder in due course and the maker becomes liable to the holder. It necessarily follows that the maker's liability to the bank ceases. If this were not true the maker might obtain a discharge of his liability on the note by paying the bank even after it had transferred its rights by endorsement of the note to a bona fide holder.

To hold that the maker of a note continues liable to a national bank for money borrowed, after the bank has rediscounted the note, would be equivalent to holding that a negotiable promissory note loses its negotiability when discounted for the maker by a national bank. There is clearly no legal justification for such a conclusion.

It has been suggested that the position taken in the opinion under consideration constitutes a radical departure from previous rulings of the Comptrollers office.

It is true that for many years it was customary for national banks to continue to carry as assets notes which had been rediscounted. This practice, which necessarily resulted in a duplication of the assets of national banks, has, however, been discontinued and while the reports of condition now show the amount of bills or notes rediscounted these amounts are not included in the total assets of the bank.

It necessarily follows that unless a note remains an asset of a bank after it has been rediscounted it does not constitute a liability of the maker to the bank but becomes a liability of the maker to the bona fide holder.

This principle has been consistently recognized by the Comptroller's office in the administration of the estates of failed banks. The maker of a note held by a failed bank is ordinarily entitled to offset his deposit balance with the bank against the note but in the administration of receiverships the Comptroller has consistently declined to allow the maker of a note to offset his deposit balance if the note is not in the hands of the receiver but is held by some other bank under rediscount on the ground that he may thereby obtain preference over other creditors to the extent of the offset if the estate of the bank is insufficient to pay the depositors in full. This question was involved in the case of United States Bank v. McNair, 116 N. C. 550; 21 S. E. 389. In that case the maker of the note was endeavoring to have his liability treated as a liability to the bank in order to obtain the benefit of an offset but the court disallowed his claim.

With all due deference to the opinion of those who have taken exception to this ruling of the Board, the fear that it may be successfully used by banks to evade the limitations of Section 5200 seems to be very much exaggerated.

So long as the customer's paper is well secured or is of such intrinsic value as to find a ready market with other banks the contingent liability incurred by the endorsing bank is not of serious consequence. On the other hand, if the paper offered for rediscount is not intrinsically valuable and the offering bank is merely seeking to evade the limitations of Section 5200, it is not likely that other banks would feel disposed to rediscount such paper. They would in such case be much more likely to require the borrowing bank to execute its note secured by its customer's note with a proper margin, in which case the customer's paper would remain the property of the borrowing bank and would have to be included in the liabilities of the makers to the borrowing bank. If the borrowing bank, in order to evade the limitations of Section 5200, should enter into an agreement with its correspondent to repurchase rediscounted paper before maturity, or to leave the proceeds of the rediscount on deposit with it, the transaction would not have been entered into in good faith and an examiner or officers of a Federal reserve bank would be justified in treating such paper as subject to the limitations of Section 5200.

As stated by Daniel on Negotiable Instruments (Section 779-b, Volume 1, Sixth Edition)-

> "Under several provisions of the statute (Negotiable Instruments Law), it is held that merely giving the transferrer credit does not constitute the transferee a holder in due course. Thus when a bank simply discounts a note and credits the amount thereof on the endorser's account, without paying to him any value for it, such bank is not a purchaser for value or a holder in due course as defined by the statute". (Albany County Bank v. People's Co-operative Ice Co., 86 N. Y. S. 772, 92).

If, however, a bank negotiates a note of its customer in good faith in order to obtain additional funds to take care of the needs of other customers, there would seem to be no justification for treating the liability of its customer to the bona fide holder of the note as a liability to the bank itself. The fact that the bank is contingently liable as endorser and may be called upon to pay the note if the maker defaults should very properly be taken into consideration in determining liabilities that may be incurred by the bank under Section 5202 but should not be taken into consideration in determining the liabilities that may be incurred to the bank under Section 5200.

The Board has heretofore ruled that a national bank may lend to one customer an amount equal to ten per cent of its capital and surplus and may thereafter accept drafts of the same customer under authority of the Federal Reserve Act. In this case the bank assumes a direct and not a contingent liability on the drafts accepted and is the primary obligor. This fact, however, does not justify the Board in requiring banks to treat this liability assumed by the bank as a liability of its customer to the bank for borrowed money within the meaning of Section 5200.

If the Board feels that it is necessary to take any affirmative action to prevent its ruling from being used by member banks as a means of evading the limitations of Section 5200, it is suggested that it might amend Section III of Regulation "A", series of 1917, to read substantially as follows:

III. Applications for Rediscount.

> "All applications for the rediscount of notes, drafts or bills of exchange, must contain

a certificate of the member bank in form to be prescribed by the Federal reserve bank, that to the best of the knowledge and belief of the officers of the applicant bank, such notes, drafts or bills of exchange have been issued for one or more of the purposes mentioned in 2 (a); such certificate shall also show whether the notes, drafts or bills discounted for any one borrower whose paper is offered for rediscount, exceeds ten per cent of the capital and surplus of the applicant bank, including notes, drafts or bills held in its own portfolio or under rediscount with other banks.

If the aggregate of such notes, drafts or bills does exceed ten per cent of the capital and surplus of the applicant bank, such certificate shall show (a) the amount held in its own portfolio, (b) the amount rediscounted with other banks, (c) the amount and character of security held, (d) whether or not the member bank is under agreement to repurchase at or before maturity notes, drafts and bills rediscounted, (e) whether or not it has received the actual proceeds of notes, drafts and bills rediscounted or merely a book credit therefor."

With this regulation in force, the Federal reserve bank would be able to determine the amount of secured and unsecured paper discounted by the applicant bank for any one borrower and rediscounted with other banks. If properly secured, the contingent liability of the member bank on the paper rediscounted in good faith would constitute merely a nominal liability. On the other hand, if the intrinsic value of the paper rediscounted appeared to be such as to make it more than probable that the endorsing member bank would be called upon to pay it, the Federal reserve bank could in its discretion determine whether such paper though technically eligible should be accepted for rediscount by the Federal reserve bank.

The Comptroller of the Currency might in like manner require national banks to show in their reports of condition information called for in the Regulation of the Board as amended in accordance with the foregoing suggestion.

The National Bank Examiner might likewise require the officers of the national bank to certify on oath whether the bank is under agreement to repurchase rediscounted paper and whether it has received the proceeds of such paper or merely a book credit and, for reasons hereinbefore stated, might treat all paper rediscounted under an agreement to repurchase or for which merely book credits have been received, as subject to the limitations of Section 5200.

Respectfully,

M. C. Elliott,

Counsel.

Hon. W. P. G. Harding,
Governor,
Federal Reserve Board.

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

3323

July 23, 1918.

X-1086

Hardee

Dear Sir:

The attention of the Board has been called to the large amount of detail work in connection with discount operations between Federal Reserve banks, and, with the desire of doing something to lighten the work, the Board has had under consideration a suggestion which was made at a recent conference with the Governors of Federal Reserve banks. It is hoped that some method, consistent with law and with the regulations of the Board, can be devised which will simplify the operation, but as to the question whether under authority of a provision in Section 14 of the Act a Federal Reserve bank may discount a fifteen day note of another Federal Reserve bank secured by eligible paper, the Board has reached a definite conclusion. The provision referred to is as follows:

> (Section 14) * * * * * * (a) To deal in gold coin and bullion at home or abroad, to make loans thereon, exchange Federal Reserve notes for gold, gold coin, or gold certificates, and to contract for loans of gold coin or bullion, giving therefor, when necessary, acceptable security, including the hypothecation of United States bonds or other securities which Federal Reserve banks are authorized to hold."

If a transaction should be entered into in good faith by a Federal Reserve bank in order to obtain a loan of gold coin or bullion, the evidence of such loan might take the form of a fifteen day note and might be secured by United States bonds or other securities, including eligible paper.

Section 14, however, relates to open market operations of a Federal Reserve bank as distinguished from discount transactions engaged in with member banks and with other Federal Reserve banks. Section 13 relates to rediscount operations with member banks and the provision for such operations as between Federal Reserve banks is found in Section 11.

Indexed Copy filed 332.5

Any transaction, therefore, between Federal Reserve banks which is to all intents and purposes intended as a rediscount operation, should be consummated in accordance with the provisions of these two sections. There is no authority given in Section 11 for a Federal Reserve bank to make its own note secured by eligible paper, but the Federal Reserve Board is authorized and empowered merely (Section 11-b) "To permit, or, on the affirmative vote of at least five members of the Federal Reserve Board to require Federal Reserve banks to rediscount the discounted paper of other Federal Reserve banks at rates of interest to be fixed by the Federal Reserve Board."

Some years ago this same question was considered in connection with the rediscount of member banks' notes secured by eligible paper, and the conclusion was reached that the statute as itthen stood did not authorize the discount of a fifteen day collateral note made by a member bank. In order to make such transactions possible, the Act was amended so as to authorize the Federal Reserve banks to discount notes of member banks having not longer than fifteen days to run, when secured by eligible paper or by obligations of the United States.

The Board is unable to find any authority for the use of notes made by Federal Reserve banks, no matter how secured, in rediscount operations between Federal Reserve banks, and in its opinion the Act would have to be amended to make such transactions permissible.

Very truly yours,

Governor.

The Governor,
Federal Reserve Bank,

FEDERAL RESERVE BOARD

WASHINGTON

MJ/JCO

April 6, 1918

X-871

Dardea

Dear Sir:

The "War Finance Corporation" Act which was signed by the President on April 5, provides among others that no stamp or tax shall be required or imposed upon a promissory note secured by bonds or obligations of the United States issued since April 24, 1917, or secured by the pledge of a promissory note which itself is secured by the pledge of such bonds or obligations: Provided, That in either case the par value of such bonds or obligations shall equal the amount of such note.

In view of the above change in law it will no longer be necessary to affix revenue stamps to member banks' collateral notes secured by Liberty Loan bonds or U. S. Certificates of Indebtedness.

It is suggested, therefore, that the practice of purchasing Liberty Bonds and Certificates of Indebtedness under so-called repurchase agreements be discontinued and that such borrowing by member banks be made on their own promissory notes secured by such bonds and certificates.

Paragraphs 1 and 2 of our letter X-795 of March 12 may also be disregarded and the new code words on form 34 "BUCK" and "BOON" may be eliminated as soon as the bonds and certificates now held under repurchase agreements mature. Future borrowings secured by War obligations should be reported on schedules of "Bills discounted--members" - BD 4 and against memorandum items "MAZE" and "MIST" on Form 34 as member banks' collateral notes or customers' paper secured by Liberty bonds and certificates of indebtedness. Discounts of commercial paper taken under repurchase agreement may be reported as heretofore in accordance with instructions found in the last paragraph of our mimeograph letter X-795 of March 12.

Very truly yours,

Secretary.

Federal Reserve Agent,

MEMORANDUM FOR THE SECRETARY.

Under the new Finance Corporation Act member banks' collateral notes are tax or stamp-free when secured by U. S. Liberty bonds and certificates of indebtedness. Member banks call notes secured by commercial paper apparently must pay the 2¢ per $100 tax.

Under date of December 1 the Federal Reserve banks were instructed to make short-time advances on eligible commercial paper of longer maturities under so-called repurchase agreements. The banks have availed themselves of this privilege and have been taking such paper in some volume at the 15-day rate, thus avoiding the payment of the stamp tax.

It is evident that it is the intention of Congress to tax member banks' collateral notes when not secured by Government War obligations, and that a continuation of the practice authorized in circular letter of December 1 may be found in conflict with the Act just passed.

112.24

May I ask that this matter be brought to the attention of the Board so I may be advised of its stand in the matter, since we must inform the Banks at once as to the proper mode of reporting short-time advances secured by War obligations on the one hand and by customers' paper on the other.

Respectfully submitted,

M. Jacobson
Statistician.

April 5, 1918.

MJ-AAM

March 12, 1918

Dear Sir:

Some of the Federal Reserve banks in reporting to the Board purchases of Liberty bonds and U. S. certificates of indebtedness under so-called repurchase agreements (the selling bank obligating itself to repurchase these securities within 15 days) have been classing such transactions as 15-day advances upon members' collateral notes, instead of purchases of Government securities.

In order to insure uniform treatment of such transactions by all the banks it is requested that the purchase of such bonds or certificates be reported to the Board on Schedules of Investments Purchased, Form S-2, and that these investments be carried on Form 34 under the following, or similar heading: "U. S. Bonds, repurchase agreement", "U. S. Certificates of Indebtedness, repurchase agreement", and that in the Friday night telegrams to the Board the bonds so held be designated by code word "BUCK" and certificates of indebtedness so held by code word "BOCN".

It is also requested that commercial paper of the several maturities when taken by the Federal Reserve banks under an agreement with the rediscounting bank that the paper will be taken up within 15 days, shall be reported on Schedules B.D. 4 and that the words "Repurchase agreement" follow the name of the rediscounting member bank. This will insure their proper classification by our Statistical Division. At present it is difficult in some cases to determine whether the transactions represent member banks' collateral notes or paper discounted under a repurchase agreement.

Very truly yours,

Assistant Secretary.

Mr.
Federal Reserve Agent,

Washington, February 13, 1918.

Memorandum.

The object of this memorandum is to outline briefly some of the most important points of difference, in substance and effect, between the so-called "Calder Bill" and the War Finance Corporation.

(1) The Calder Bill would give power to Federal Reserve Banks to rediscount member banks' notes secured by "such bonds or notes of any railroad, industrial, public utility corporation or municipality as the Federal Reserve Board upon investigation deems a proper security for the Federal Reserve Banks to receive as collateral." For the purposes of this memorandum, we must assume, of course, that if the bill were passed the Federal Reserve Board would permit the rediscount of member bank notes secured by such collateral. Upon that assumption, it is clear that billions of outstanding securities would become directly available as collateral for advances by Federal Reserve Banks, and indirectly available as security for Federal Reserve notes. It would not be a question of dealing only with new financing "compatible with the public interest at this time", or with the renewal of maturing obligations, but the whole mass of securities already outstanding would become available without any power of differentiation at all as to whether or not they are serving the public interest at this time. The proceeds of such borrowing could be used for anything - compatible or incompatible. It is un-

necessary to elaborate the importance of this point.

(2) Granting that most of the securities covered by the Calder Bill amendment are either unsalable today or could be sold only with substantial concessions, even as against the present heavily reduced prices, the Calder Bill does not have for its object to find a means of thawing out these frozen securities. The only solution that the Calder Bill provides is that holders of securities, either directly or indirectly, pledge them against advances to be secured from Federal Reserve Banks. The Finance Corporation, on the other hand, provides ways and means by which the appeal should be made not exclusively to the Federal Reserve System but to the securities market in general. By substituting, in effect, the short term bond for the unsaleable security of industrial corporations, public utilities, railroads or municipalities, or by substituting these short term bonds for the maturing obligations of such corporation, a new security is offered which will have a general marker, first, because it will be considered a Government security, and, second, because of the fact that some provision is made, in case of emergency, to use these bonds as collateral for borrowings from Federal Reserve Banks. To make this point clear: Suppose that an electric company has maturing bonds amounting to ten million dollars; it wants to offer instead a five year electric note but finds it impossible to place the same. Under the Calder Bill, all that could possibly be done would be to borrow the full amount from the Federal Reserve Bank. Under the plan of the War Finance Corporation, five year bonds of that corporation would be issued and either

taken in exchange by the holders of the old, maturing electric notes, or the new five year short term bonds could be placed on the market and the proceeds used to pay off the maturing notes. In other words, the Finance Corporation should have the tendency of reopening the security market for now unsaleable securities, so that new elasticity will be given the securities market instead of regarding this market as hopelessly dead and instead of using the Federal Reserve System, an instrument created for the protection of commercial paper, as a market upon which to unload unsaleable securities.

(3) It is safe to conclude from the above that the amount of paper secured by War Finance Corporation bonds expected to be rediscounted with Federal Reserve Banks would be much smaller than the amount likely to be borrowed from the Federal Reserve System in the case of the Calder Bill, not only because, in the first case, the absorbing power of the security market acts as a buffer and only what the security market cannot take - and what, after that, the banks cannot carry - will go into the Federal Reserve System, but also, as stated under (1), because the output of the short term bonds by the War Finance Corporation is restricted to definite purposes of the present emergency, while, under the Calder Bill, the only possible assistance would have to come through the Federal Reserve System, and all securities issued during past generations would become available as collateral without any scrutiny as to the objects for which they have been issued.

(4) If we have these points clearly in mind, it is incomprehensible why the hue and cry of inflation should be raised against the Finance Corporation by the very people who, apparently, are in favor of the Calder Bill. As a matter of fact, as above stated, we would have to expect a much larger degree of inflation under the Calder Bill than under the proposed War Finance Corporation legislation. Are we not driven to the logical conclusion that these critics of the War Finance Corporation bill are opposed to it because it restricts inflation so much more than the Calder Bill rather than because they are generally apprehensive of too much inflation to be caused by the contemplated legislation?

Paul M. Warburg.

January 31, 1918.

Dear Mr. Secretary:

In the absence of Governor Harding, I am replying to your letter of January 22nd enclosing letter from the Manufacturers National Bank of Troy, New York, suggesting that the law be amended so as to permit Federal Reserve Banks to discount their member banks' notes secured by government bonds having thirty days to run, instead of the present limit of fifteen days. 1/19/18

The Board has fully discussed this matter, and is rather adverse to such an amendment, as it would, in all probability, be difficult to keep the use of the fifteen-day notes secured by government bonds within reasonable limits. As we can always permit the banks to renew their notes, it was thought better to let the law stand as it is at present, and not to urge an amendment along these lines. For the present, at least, there does not appear to be an urgent necessity for it.

Very truly yours,

Vice Governor.

Hon. Russell C. Leffingwell,
Assistant Secretary of the Treasury.

332.3

No. 2. S Date Jan. 30, 1918. 272.

FEDERAL RESERVE BOARD

MEMORANDUM.

For Mr. Harding

At a meeting of the Federal Reserve Board on Jan. 30, the following matter was referred to you (as Chairman, Committee on / as member, " " / as), for reply.

The attached letter of the Manufacturers National Bank of Troy relative to the use of Government bonds as collateral against bills, 11/9/18

W P G Harding
Secretary.

Please return this memorandum with copy of documents resulting from action taken, if any,

Date 1/31/18

Documents attached hereto

Signature B.

TREASURY DEPARTMENT

WASHINGTON

3323

January 22, 1918.

Docket Jan. 28

RECEIVED
JAN 24 1918
GOVERNOR'S OFFICE

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

My dear Governor Harding:

1/19/18

I am transmitting herewith a letter from the Manufacturers National Bank of Troy, N. Y., for your consideration.

Respectfully,

Assistant Secretary of the Treasury.

721

THE MANUFACTURERS NATIONAL BANK TROY, N.Y.

FRANK E. HOWE, PRESIDENT
ALBA M. IDE, V. PREST. EDWARD MURPHY, V. PREST.
HARRY E. POLLARD, V. PREST. WILLIAM C. FEATHERS, CASHIER
WILLIAM F. SEBER, ASST. CASHIER

January 19,1918

Hon Wm. G Mc Adoo,

Secretary of the Treasury,

Washington, D.C.

Dear Sir:

Looking forward to the next sale of the Liberty Loan Bonds and applying our own resources and facilities to the largest possible subscription for our own account, I reach the conclusion that we would be greatly helped in our endeavor, if it were possible to use the bonds, which we paid for, with the Federal Reserve Bank as collateral to bills payable of the Bank, for a longer period than the present allowed term of fifteen days, and if such loans can be made without the use of revenue stamps.

Many other banks may be positioned as we are and their interest to co-operate in this matter would undoubtedly be raised if an amendment to the law could preceed the next issue, which would allow the longer term for borrowing and freedom from revenue stamps. The Governement can protect itself through the rate charged upon the loan.

Asking your consideration to this suggestion beg leave to remain,

Respectfully yours,

F E Howe
President.

December 27, 1917.

Mr. E. P. Wharton,
President Greensboro National Bank,
Greensboro, N. C.

Dear Sir:-

The Secretary of the Treasury has referred to this office for reply your letter of December 6th with reference to the loss which may be occasioned your bank because of the fact that the notes which you will have to give to the Federal Reserve bank in order to carry your subscription to Treasury certificates for $500,000 will have to be stamped and renewed every fifteen days.

The Board is informed that the situation with respect to these notes cannot be relieved except by an amendment to the present revenue act, and as you know, the Federal Reserve Act limits the maturity of member banks' collateral notes to fifteen days. The Commissioner of Internal Revenue advises that he is without authority to waive any of the requirements of the revenue law and the only suggestion that the Board can make is that you take the matter up with the Federal Reserve Bank of Richmond, as it is possible that it may be able to suggest some method of extending you desired accommodations which will not involve repeated liability to the stamp tax.

Very truly yours,

Governor.

3323.3

December 18, 1917

AGJCP
MGH

Mr. E. P. Wharton, President,
The Greensboro National Bank,
Greensboro, N. C.

Dear Sir:

I am in receipt of your letter of December 6th with reference to the loss which may be occasioned to your bank because of the fact that the notes which you will have to give to the Federal Reserve Bank in order to carry your subscription to Treasury certificates for $500,000 will have to be stamped and renewed every fifteen days.

I regret that the situation with respect to these notes can not be relieved, but the statute limits the maturity of such notes to fifteen days, and this Department is without authority to waive this provision.

I would suggest, however, that you take up the matter with the Federal Reserve Bank, as it may be that the accommodation which you desire can be extended in some other manner which will not involve repeated liability to the stamp tax.

Respectfully,

Secretary.

AGJCP
MGH

TREASURY DEPARTMENT

3323

WASHINGTON

December 18, 1917

Mr. E. P. Wharton, President,
The Greensboro National Bank,
Greensboro, N. C.

Dear Sir:

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I would suggest, however, that you take up the matter with the Federal Reserve Bank, as it may be that the accommodation which you desire can be extended in some other manner which will not involve repeated liability to the stamp tax.

Respectfully,

Secretary.

THE COMMISSIONER OF INTERNAL REVENUE

33213

December 10, 1917.

Mr. Peacock:

Mr. Roper would like for you to dictate a letter on this matter, for ~~his~~ Secretary's signature.

12/27/17 E. G. B.

Take up rediscount com. paper with an stat banks notes to 10 days & he is without authority to authorize par to be waived

A/JCP OK
MOS

Capital $100,000.00

THE GREENSBORO NATIONAL BANK

E. P. WHARTON, President — NEIL ELLINGTON, Vice-President and Chairman of Board — A. H. ALDERMAN, Cashier

DEPOSITARY FOR CITY OF GREENSBORO, COUNTY OF GUILFORD, U. S. GOVERNMENT

3232.3

GREENSBORO, N. C.
Dec. 6th. 1917.

Hon. Wm. G. McAdoo,
Secretary of the Treasury,
Washington, D. C.

Dear Sir:-

Our bank has been co-operating in every way possible in the sale of Liberty Bonds, subcriptions to Treasury Certificates, etc., and we expect to continue. In the last issue of Bonds our allottment was $124,000.00, and we sold considerably over $400,000.00. When the last offer came to subscribe to Treasury Certificates due June 15th. we subscribed to $500,000.00. Of course, this money goes on deposit to us until called for. We figured that we could come out without any loss on this, but overlooked the fact that the notes that we will have to give the Federal Reserve Bank to carry this proposition will have to be stamped and renewed every fifteen days.

As you stated to me, when passing through Greensboro, in connection with this loan only being made fifteen days, that you would see that they were renewed, and you were kind enough to attend to this immediately, so that we had no trouble in handling notes in connection with the Liberty Bonds. Now when the Government calls on us for this money that is on deposit, if we could give a note at that time, secured by these Treasury Certificates, to run until June 15th., so that we would not have to stamp it but once, it would keep us from suffering any loss on account of the subscription to the Treasury Certificates. But if we have to stamp them every fifteen days there would be a considerable loss.

As I took the personal responsibility of making this large subscription I would be glad to have a letter from you that I can show at the next Directors Meeting.

Yours very truly,

E P Wharton President.

November 10, 1917.

Dear Dr. Miller:

At our conference with the Governors yesterday and day before yesterday, the question of the renewal of fifteen day notes came up quite repeatedly, and reference was made to the letter on page 879 of the Bulletin concerning renewal of short term paper, which had opened the question but had not closed it, inasmuch as it contained a permission to grant exceptions and closed by saying, "The matter has been referred to the proper committee of the Board for report and a circular will be sent to all Federal reserve banks on the subject within the next few days."

The report of the committee was submitted and adopted by the Board and it was that report which had been suggested for publication in the Bulletin instead of the letter. It would have been an easy matter to give this report the form of a letter so that it would have the form of an informal ruling, and gone out as such. The question was raised, however, ad nauseam, that this was not an informal ruling but a report, and finally, having given away to this technical objection, an incomplete letter was published rather than a complete memorandum; and as it stands now, we have again to follow up this matter by the memorandum, in view of the

fact that the letter printed in the Bulletin announced the coming of the same. It is unnecessary to say that the memorandum will fall flat if now published in the December number in reply to a letter of September twelfth. To my mind, it subjects the Board to ridicule if it takes so long to take it to give an answer to a simple memorandum in answer to a simple question.

Very truly yours,

Hon. A. C. Miller.

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N.
3323

October 26, 1917.

Mr. E. P. Wharton,
Greensboro, N. C.

My dear Sir:

Secretary McAdoo told me this morning that you were under the impression that fifteen-day notes of member banks of the Federal Reserve system which are secured by United States bonds, will not be renewed by the Federal Reserve bank. I called up Mr. Seay, Governor of the Federal Reserve Bank of Richmond over the telephone upon receipt of this information, and he advises me that this is not the case as far as his bank is concerned. The Board has made no such ruling, and while the law limits direct accommodations to member banks upon their own notes to fifteen days, it is silent as to renewals, and the policy of all the Federal Reserve banks has been to make renewals in meritorious cases.

A member bank can rediscount with the Federal Reserve bank a note of a customer secured by United States bonds running as long as ninety days at a time, and I would suggest that you communicate with the officials of thexFederal Reserve Bank of Richmond asking them to state definitely their policy regarding renewals of member banks' notes which are secured by United States bonds. Governor Seay assures me that he will take pleasure in correcting your misapprehension.

Very truly yours,

Governor.

231

REPORT

Washington, October 4, 1917.

Federal Reserve Agent Wellborn's comment on renewal of fifteen day notes.

P. M. W.

The question has been referred to the Committee on Investments what attitude Federal Reserve Banks should take with respect to renewals of fifteen day notes. This question was raised by Mr. Wellborn and I believe Governor Harding has already answered it.

If the question is to be answered as a general one, I think that the committee would give it as its opinion that when a fifteen day note expires, circumstances may, of course, prevail which would render its renewal perfectly legitimate, and there can, therefore, be no thought of establishing any general rule that renewals should be refused. (The "renewal" in that case means the giving of a new fifteen day note secured by the same or different collateral.) If, however, a Federal Reserve Bank should observe that new fifteen day notes are used with a definite intention of avoiding rediscounting the 60 or 90 day paper so as to profit by the lower fifteen day rate as against the 60 or 90 day rate, then Federal Reserve Banks should inform the borrowing banks that their requests for fifteen day accommodation will be refused and that if these banks desire accommodation they should rediscount the 60 or 90 day paper serving as collateral.

It is not believed that it would be possible to give more than this general suggestion to our Federal Reserve Banks.

Respectfully submitted:

Paul M. Warburg

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Form 40

TELEGRAM

FEDERAL RESERVE BOARD

WASHINGTON

#770

K

June 19, 1917. 3323

3323

Sawyer,
Federal Reserve Agent,
Kansas City, Mo.

Amendments make fifteen day paper eligible as collateral against Federal reserve notes but are not yet signed by President.

#10

Treasury Department

TELEGRAM

44WU MO 22 Govt

KANSAS CITY Mo 1037am June 19 1917

Federal Reserve Board

Washington D.C.

Do amendments as passed make fifteen day paper eligible as collateral against Federal Reserve notes

Sawyer, Agent

12noon

FEDERAL RESERVE BOARD

WASHINGTON

May 31, 1917.

Dear Mr. Warburg :

Section 16 of the Federal Reserve Act provides that the collateral offered by Federal reserve banks as security for the issue of Federal reserve notes shall be "notes, drafts, bills of exchange, or acceptances rediscounted under the provisions of Section 13 of this act",etc.

If, therefore, a Federal reserve bank rediscounts for any member bank, as it is authorized to do under the provisions of Section 13, any notes, drafts or bills of exchange drawn for the purpose of carrying or trading in bonds, or notes, of the United States, such notes, drafts, or bills of exchange are clearly eligible as collateral security for Federal reserve notes.

Respectfully,

W. P. G. Harding.

Honorable Paul M. Warburg,
Vice Governor, Federal Reserve Board.

Bulletin for June 1917

File

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May 21, 1917.

Memorandum for Mr. Warburg:

The Federal Reserve Board has established 15-day paper rates as follows:

10 May 7, Kansas City, 3% on "15-day notes secured by Government bonds or certificates."

9 May 8, Minneapolis, 3% on "15-day notes secured by Government obligations - effective at once."

4 May 10, Cleveland, 3% on "15-day notes of member banks secured by U.S. Treasury certificates of indebtedness, effective May 10,"

3 May 10, Philadelphia, 3% on "all classes of paper with a maturity of 15 days or less."

7 May 19, Chicago, 3% on "member banks' 15-day promissory notes secured by Government bonds,"

The Board has also informed the Federal Reserve Bank of San Francisco under date of May 19 (in reply to an inquiry from that bank) of its action in the case of the other banks.

Secretary.

FEDERAL RESERVE BOARD

WASHINGTON

k

May 21, 1917.

Memorandum for Mr. Warburg:

The Federal Reserve Board has established 15-day paper rates as follows:

May 7, Kansas City, 3% on "15-day notes secured by Government bonds or certificates."

May 8, Minneapolis, 3% on "15-day notes secured by Government obligations - effective at once."

May 10, Cleveland, 3% on "15-day notes of member banks secured by U.S. Treasury certificates of indebtedness, effective May 10."

May 10, Philadelphia, 3% on "all classes of paper with a maturity of 15 days or less," effective May 10

May 19, Chicago, 3% on "member banks' 15-day promissory notes secured by Government bonds," effective at once

The Board has also informed the Federal Reserve Bank of San Francisco under date of May 19 (in reply to an inquiry from that bank) of its action in the case of the other banks.

H Parker Willis
Secretary.

Frisco, Chicago, N.Y., Philadelphia, Boston, Dallas

Form 40

TELEGRAM

FEDERAL RESERVE BOARD

WASHINGTON

~~332.3~~

332.3

Draft telegram to May 7, 1917.

Federal Reserve Bank, Kansas City
Federal Reserve Bank, Minneapolis

Board approves rate of three per cent. for member banks fifteen day notes secured by Government bonds or certificates. This rate is given to meet a temporary situation and must be understood to be subject to revision.

Willis, Secretary.

OFFICIAL BUSINESS
GOVERNMENT RATES
CHARGE FEDERAL RESERVE BOARD

2—7729

February 21, 1917.

Mr. T. D. Webb,
Vice President Fourth and First National Bank,
Nashville, Tenn.

My dear Sir:

2/17/17

I have received your letter asking if you could discount your bank's note with the Federal Reserve Bank of Atlanta secured by certain bonds described therein.

In reply, I would refer you to an act amending the Federal Reserve Act, approved September 7, 1916, from which I quote:

> "Any Federal Reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal Reserve Banks, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible for rediscount or for purchase by Federal Reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States."

You will see from this that your note secured by the bonds described would not be acceptable to a Federal Reserve Bank as the collateral is limited to bonds or notes of the United States, and to such notes, drafts, or bills of exchange or bankers' acceptances as are eligible for rediscount or puchase by Federal Reserve Banks under the provisions of the Act. The securities described in your letter are of an investment character and notes based upon investment transactions are excluded under the provisions of Section 13.

Very truly yours,

Governor.

FOURTH AND FIRST NATIONAL BANK

3323

NASHVILLE, TENN. Feb. 1917.

2/17/17
given date

Mr. W. P. G. Harding, Chairman,
Federal Reserve Board,
Washington, D.C.

My Dear Sir:

In the event we should desire to make a loan with the Federal Reserve Bank in Atlanta, could we use our note, collateraled with good and substantial bonds, of the following class:

Argentine Government 5% notes, due March 1, 1917,
" " 6% Treasury Bonds, due May 15, 1920,
Baltimore & Ohio R.R. 5% refunding and general mortgage, due Dec. 1, 1925,
Bell Telephone Co. of Canada, 5% Bonds, due April 1, 1925,
Canadian Consolidated Rubber Co. 5% debentures, due Dec. 1, 1918,
Canadian Northern Railway, 5% 2-year collateral bonds, due Sept. 1, 1917,
Chicago Railways, 1st mortgage 5% gold bonds, due February 1, 1927,
Cumberland Telephone & Telegraph Co., 1st and Gen. closed mtg bonds, due 1937,
Interborough Rapid Transit, first refunding mortgage, due 1966,
City of Nashville, Tenn., Street Improvement and Sewer 4% bonds, due 1926.

Awaiting your reply, I remain, with kindest regards,

Yours very truly,

Vice President.

HW

Ans. Feb. 21, 1917

2/21

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332.3

LIBERTY LOAN DISCOUNT RATES.

Bank	Customers' Paper			Banks' Direct Obligations		
	Rate	Maturity	Effective	Rate	Maturity	Effective
Boston	3½%	90 days	June 11			
New York	3½%	"	May 22			
Philadelphia	3½%	"	June 1	3½%	15 days	June 11
Cleveland	3½%	"	June 15	3%	15 days	June 8
Richmond	3½%	"	May 25			
Atlanta	3½%	"	May 24			
Chicago	3½%	"	May 24	3%	"	May 19
St. Louis	3½%	"	May 25			
Minneapolis	3½%	"	June 4	3%	"	May 8
Kansas City	3½%	"	May 28	3%	"	May 7
Dallas	3½%	"	May 22			
San Francisco	3½%	"	May 23			

Elliott

COPY

332.3

October 5, 1916.

332.3

My dear Governor:-

This office has been asked for an opinion on the question of whether or not a Federal reserve bank may make advances to its member banks on their promissory notes secured by county warrants.

Section 13 of the Federal Reserve Act, as amended by the Act approved September 7, 1916, provides in part as follows:

> "Any Federal reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days ********** provided such promissory notes are secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States".

This section specifies in detail the forms of security which may be accepted by Federal reserve banks as collateral security for bills payable discounted for member banks.

It will be observed that county warrants are not included in the list of securities mentioned. It is significant that while municipal and county warrants are dealt with elsewhere in the Act, in the same section in which United States bonds are made eligible for purchase by Federal reserve banks United States bonds are mentioned in the foregoing provision while county warrants and municipal securities are omitted.

In the opinion of this office, therefore, there is neither expressed nor implied authority for a Federal reserve bank to make advances to any of its member banks on promissory notes secured by county warrants.

Respectfully,

(Signed) M. E. ELLIOTT

Counsel.

Hon. W. P. G. Harding,
Governor.

FEDERAL RESERVE BOARD

WASHINGTON

September 11, 1916.

Mines 797

Dear Sir:

The amendments to the Federal Reserve Act approved on September 7, 1916, provide in part that -

"Any Federal reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States".

The Federal Reserve Board does not deem it necessary to promulgate any special ruling relating to the exercise of the powers conferred by this amendment, but it is expected that each Federal reserve bank will establish rates, to be approved by the Federal Reserve Board, at which it will make advances on promissory notes of member banks properly secured. It is suggested, however, that those banks which have established a ten-day discount rate on commercial paper abolish the ten day rate and make a uniform fifteen day rate for both commercial and member bank paper rather than a ten day rate for commercial paper and a fifteen day rate for advances on collateral notes of member banks.

As soon as such rates are established and approved you will no doubt inform your member banks of the facilities afforded under the provisions of this amendment, stating the rate at which you are prepared to make advances on their promissory notes, and calling their attention to the fact that such notes must be secured either by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or purchase by Federal reserve banks, or by the deposit or pledge of bonds or notes of the United States.

Very truly yours,

Governor.

.0/5 Memo 797 332.3

Dear Sir:- Draft of letter to all Federal Reserve Banks. September 11, 16

The amendments to the Federal Reserve Act approvrd on September 7, 1916 provide in part that-

"Any Federal reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States."

The Federal Reserve Board does not deem it necessary to promulgate any special ruling relating to the exercise of the powers conferred by this amendment, but it expects that each Federal reserve bank will establish rates, to be approved by the Federal Reserve Board, at which it will make advances on member bank promissory notes properly secured. It is suggested, however, that those banks which have established a ten-day discount rate on commercial paper abolish the ten day rate and make a uniform fifteen day rate for both commercial and member bank paper rather than a ten day rate for commercial paper and a fifteen day rate for advances on member bank collateral notes of paper.

As soon as such rates are established and approved will you please inform your member banks of the facilities afforded under the provisions of this amendment, stating the rate at which you are prepared to make advances on their promissory notes, and calling their attention to the fact that such notes must be secured either by such notes, drafts bills of exchange, or bankers' acceptances, as are eligible for rediscount or purchase by Federal Reserve Banks; or by the deposit or pledge of bonds or notes of the United States.

Very truly yours,

Governor.