Bankers Acceptances
New Eligibility Regulation

To each Bank, Trust Company and Other Accepting Banker
in the Second Federal Reserve District:

In transmitting copy of Federal Reserve Board Regulation A, Series of 1922, ( superseding Regulation A, Series of 1920) we desire to call to your attention the modification of regulation with regard to the rediscount by Federal Reserve Banks of bankers acceptances drawn to finance export and import transactions. The effect of the modification eliminates certain requirements respecting such acceptances contained in previous regulations.

We also direct your particular attention to the comments of the Federal Reserve Board, contained in its letter of March 29, 1922, accompanying the regulation. From it you will observe that responsibility is placed more directly than heretofore upon Federal Reserve Banks to pass upon the eligibility of import and export acceptances.

To avoid possible misunderstanding and resulting embarrassment, you are invited and requested to consult with officers of this bank with respect to credits from time to time under consideration involving any question of eligibility.

Very truly yours,

BENJ. STRONG,
Governor
Washington, March 29, 1922.

The Federal Reserve Board transmits herewith Regulation A, Series of 1922, superseding Regulation A, Series of 1920.

No change has been made in the regulation except in that part which deals with bankers' acceptances growing out of the importation or exportation of goods, and that part has been simplified by the elimination of certain matter which appeared in the former regulation. It should be understood, however, that the Board's action in issuing the new regulation with this matter eliminated does not imply any change of view as to the meaning or proper construction of the law, or as to the broad principles which should govern the exercise of the acceptance privilege. The Board is not reversing or in any way modifying any of its former rulings as to bankers' acceptances growing out of the importation or exportation of goods in so far as these rulings have been interpretative of the law, or have laid down broad general principles, the observance of which is, as a result of long experience in the field of international banking, recognized as essential in the proper conduct of the acceptance business. The Board's action is intended merely to allow greater latitude to Federal Reserve Banks for the exercise, each in its own way, of their discretion and judgment, observing always, of course, the express and implied limitations of the law.

Conditions affecting foreign trade at the present time are essentially different from those which led to the development of the former regulations. Prior to the enactment of the Federal Reserve Act, national banks were without authority to issue bankers' acceptances, and although some State banks had that power very few of them exercised it. During the war, however, there was a rapid growth of the acceptance business, stimulated by the abnormal demand for goods and credits, and due to this rapid growth it became necessary for the Federal Reserve Board to make frequent rulings and periodically to issue regulations for the guidance of accepting banks and Federal Reserve Banks in this new field. Regulation A, Series of 1920, constituted the last definite step in the development of bankers' acceptance regulations designed primarily to meet the exigencies of the unusual conditions that existed during and for some time after the war, that regulation containing the substance of all the more important rulings previously issued by the Board.

Those American banking institutions which have large demands for acceptance credits in foreign transactions have by this time had considerable experience in this field, and the former detailed regulations are no longer thought necessary. Moreover, it is believed that the general advancement of foreign trade, with the resulting benefit to the agricultural and commercial interests which are largely dependent upon foreign markets, can be furthered most effectually at the present time by the substitution of this simpler regulation applicable to acceptances in export and import transactions.

The responsibility for passing upon the eligibility of bankers' acceptances offered to the Federal Reserve Banks for rediscount or purchase rests upon the Federal Reserve Banks themselves, and each bank should satisfy itself, in whatever way it deems appropriate, that the acceptances conform to the requirements of the law and the Board's regulation. The Federal Reserve Board will watch carefully the development of the acceptance business under this
new regulation, with a view of making any later modification that may seem necessary or advisable. The Board will call the attention of the Federal Reserve Banks to any apparent failure to comply with the law or abuse of the acceptance privilege, and the Federal Reserve Banks will in turn be expected to keep the Board closely advised in regard to acceptance practices in their districts.

W. P. G. HARDING,
Governor.

W. W. HOXTON,
Secretary.
REGULATION A.
Series of 1922.
(Superseding Regulation A of 1920.)

REDISCOUNTS UNDER SECTION 13.

ARTICLE A.
NOTES, DRAFTS, AND BILLS OF EXCHANGE.

SECTION I. GENERAL STATUTORY PROVISIONS.

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

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

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

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

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

(e) It is indorsed by a member bank.

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

No Federal Reserve Bank may discount for any member State bank or trust company any of the notes, drafts, or bills of any one borrower who is liable for borrowed money to such State bank or trust company in an amount greater than 10 per cent of the capital and surplus of that State bank or trust company, but in determining the amount of money borrowed from such State bank or trust company the discount of bills of exchange drawn in good faith against actually existing value and the discount of commercial or business paper actually owned by the person negotiating the same shall not be included.

Any Federal Reserve Bank may make advances to its member banks on their promissory notes for a period not exceeding 15 days, provided that they are secured by notes, drafts, bills of exchange, or bankers' acceptances which 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, or bonds of the War Finance Corporation.

SECTION II. GENERAL CHARACTER OF NOTES, DRAFTS, AND BILLS OF EXCHANGE ELIGIBLE.

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

(a) It must be a note, draft, or bill of exchange which has been issued or drawn, or the proceeds of which have been used or are to be used in the first instance, in producing, purchasing,
carrying, or marketing goods in one or more of the steps of the process of production, manufacture, or distribution, or for the purpose of carrying or trading in bonds or notes of the United States.

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

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

(d) It may be secured by the pledge of goods or collateral of any nature, including paper, which is ineligible for rediscount, provided it (the note, draft, or bill of exchange) is otherwise eligible.

SECTION III. APPLICATIONS FOR REDISCOUNT.

All applications for the rediscount of notes, drafts, or bills of exchange must contain a certificate of the member bank, in form to be prescribed by the Federal Reserve Bank, that, to the best of its knowledge and belief, such notes, drafts, or bills of exchange have been issued for one or more of the purposes mentioned in Section II (a), and, in the case of a member State bank or trust company, all applications must contain a certificate or guaranty to the effect that the borrower is not liable, and will not be permitted to become liable during the time his paper is held by the Federal Reserve Bank, to such bank or trust company for borrowed money in an amount greater than that specified in Section I above.

SECTION IV. PROMISSORY NOTES.

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

(b) Evidence of eligibility and requirement of statements.—A Federal Reserve Bank must be satisfied by reference to the note or otherwise that it is eligible for rediscount. The member bank shall certify in its application whether the note offered for rediscount has been discounted for a depositor other than a bank or for a nondepositor and, if discounted for a bank, whether for a member or a nonmember bank. The member bank must also certify whether a financial statement of the borrower is on file with it.

A recent financial statement of the borrower must be on file with the member bank in all cases, except with respect to any note discounted by a member bank for a depositor other than a bank or another member bank if—

(1) It is secured by a warehouse, terminal, or other similar receipt covering goods in storage, or by bonds or notes of the United States; or

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

The Federal Reserve Bank shall use its discretion in taking the steps necessary to satisfy itself as to eligibility. Compliance of a note with Section II (b) may be evidenced by a statement of the borrower showing a reasonable excess of quick assets over current liabilities. A Federal Reserve Bank may, in all cases, require the financial statement of the borrower to be filed with it.

1 When used in this regulation the word "goods" shall be construed to include goods, wares, merchandise, or agricultural products, including live stock.
SECTION V. DRAFTS, BILLS OF EXCHANGE, AND TRADE ACCEPTANCES.

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

(b) Evidence of eligibility and requirement of statements.—A Federal Reserve Bank shall take such steps as it deems necessary to satisfy itself as to the eligibility of the draft, bill, or trade acceptance offered for rediscount and may require a recent financial statement of one or more parties to the instrument. The draft, bill, or trade acceptance should be drawn so as to evidence the character of the underlying transaction, but if it is not so drawn evidence of eligibility may consist of a stamp or certificate affixed by the acceptor or drawer in a form satisfactory to the Federal Reserve Bank.

SECTION VI. SIX MONTHS' AGRICULTURAL PAPER.

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

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

ARTICLE B.

BANKERS' ACCEPTANCES.

SECTION VII. DEFINITION.

A banker's acceptance within the meaning of this regulation is defined as a draft or bill of exchange, whether payable in the United States or abroad and whether payable in dollars or some other money, of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged generally in the business of granting bankers' acceptance credits.

SECTION VIII. ELIGIBILITY.

A Federal Reserve Bank may rediscount any such bill bearing the indorsement of a member bank and having a maturity at time of discount of not more than three months, exclusive of days of grace, which has been drawn under a credit opened for the purpose of conducting or settling accounts resulting from a transaction or transactions involving any one of the following:

1. The shipment of goods between the United States and any foreign country, or between the United States and any of its dependencies or insular possessions, or between foreign countries.
2. The shipment of goods within the United States, provided shipping documents conveying security title are attached at the time of acceptance, or

A consignment of goods or a conditional sale of goods can not be considered "goods sold" within the meaning of this clause. The purchase price of goods plus the cost of labor in effecting their installation may be included in the amount for which the trade acceptance is drawn.
(3) The storage of readily marketable staples, provided that the bill is secured at the time of acceptance by a warehouse, terminal, or other similar receipt, conveying security title to such staples, issued by a party independent of the customer, and provided further that the acceptor remains secured throughout the life of the acceptance. In the event that the goods must be withdrawn from storage prior to the maturity of the acceptance or the retirement of the credit, a trust receipt or other similar document covering the goods may be substituted in lieu of the original document, provided that such substitution is conditioned upon a reasonably prompt liquidation of the credit. In order to insure compliance with this condition it should be required, when the original document is released, either (a) that the proceeds of the goods will be applied within a specified time toward a liquidation of the acceptance credit or (b) that a new document, similar to the original one, will be resubstituted within a specified time.

Provided, that acceptances for any one customer in excess of 10 per cent of the capital and surplus of the accepting bank must remain actually secured throughout the life of the acceptance, and in the case of the acceptances of member banks this security must consist of shipping documents, warehouse receipts, or other such documents, or some other actual security growing out of the same transaction as the acceptance, such as documentary drafts, trade acceptances, terminal receipts, or trust receipts which have been issued under such circumstances, and which cover goods of such a character, as to insure at all times a continuance of an effective and lawful lien in favor of the accepting bank, other trust receipts not being considered such actual security if they permit the customer to have access to or control over the goods.

A Federal Reserve Bank may also rediscount any bill drawn by a bank or banker in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange as provided in Regulation C, provided that it has a maturity at the time of discount of not more than three months, exclusive of days of grace.

SECTION IX. GENERAL CONDITIONS AS TO MATURITY OF DOMESTIC ACCEPTANCES.

Although a Federal Reserve Bank may legally rediscount an acceptance having a maturity at the time of discount of not more than three months, exclusive of days of grace, it may decline to rediscount any acceptance the maturity of which is in excess of the usual or customary period of credit required to finance the underlying transaction or which is in excess of that period reasonably necessary to finance such transaction. Since the purpose of permitting the acceptance of drafts secured by warehouse receipts or other such documents is to permit of the temporary holding of readily marketable staples in storage pending a reasonably prompt sale, shipment, or distribution, no such acceptance should have a maturity in excess of the time ordinarily necessary to effect a reasonably prompt sale, shipment, or distribution into the process of manufacture or consumption.

SECTION X. EVIDENCE OF ELIGIBILITY.

A Federal Reserve Bank must be satisfied, either by reference to the acceptance itself, or otherwise, that the acceptance is eligible for rediscount under the terms of the law and the provisions of this regulation. The bill itself should be drawn so as to evidence the character of the underlying transaction, but if it is not so drawn evidence of eligibility may consist of a stamp or certificate affixed by the acceptor in form satisfactory to the Federal Reserve Bank.

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3 A readily marketable staple within the meaning of these regulations may be defined as an article of commerce, agriculture, or industry of such uses as to make it the subject of constant dealings in ready markets with such frequent quotations of price as to make (a) the price easily and definitely ascertainable and (b) the staple itself easy to realize upon by sale at any time.