#30

The members of the Federal Reserve Board took the oath of office on August 10, 1914, immediately after the outbreak of the European war. The almost complete collapse of the world's machinery of credit forced them to give their immediate attention to the acute problems facing the country as a consequence of this catastrophe. In spite of these tasks, which absorbed their time and taxed their energies, the members of the Board, after two months, had completed the preliminary work and in particular the task of selecting the thirty-six Class "C" Directors, thus completing the boards of the Federal Reserve Banks and placing in their hands the charge of opening their respective institutions. It is hoped that, with the high spirit of public duty which inspires all those directors and the governors chosen by them the banks will open on or about November sixteenth.

It is a source of great satisfaction to the Federal Reserve Board to be able to state that the most acute phase of the emergency appears to have passed and that the main clogs in the wheels of commerce and trade have been removed. But a conflagration embracing almost all Europe must of necessity leave this country in a condition where it is our duty to organize and make available to the highest degree our own resources so as to enable us to meet our own needs and to replace the facilities suddenly withdrawn from us by the closing of the old and customary channels of credit and trade. It is the consideration of these sides of the problem that has led the Federal Reserve Board to urge the immediate opening of the banks even though it necessitated a reduction to the smallest possible scope of the program to be adopted for the opening of the banks. The Board considers it as its prime duty to set in motion the machinery for bringing the gold reserves of the

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country under a strong organization capable of centralizing available reserves, of absorbing as rapidly as possible gold wastefully circulating, and generally to increase the basis of our credit facilities.

The almost exclusive function of the Federal Reserve Banks when opening will be the receipt of the reserve deposits payable in lawful money and discounts. It is to be hoped (and all possible pressure should be brought upon member banks to that effect) that the largest possible amount of cash and preferably gold will be transferred to the Federal Reserve Banks when opening and that rediscounting operations at the start will be comparatively unimportant. Except in Districts 6 and 11 (and to a certain extent 5 and 8) where, owing to the congestion of cotton, immediate relief will be necessary, rediscounts with Federal Reserve Banks should not be encouraged, and it is thought that it will be a good policy for the Federal Reserve Banks, when opening, to fix their discount rates high enough to secure this result. It ought to be borne in mind that, for the time being, there is still a heavy cash balance due to Europe for which gold may be demanded and that Europe holds many billions of our own securities which may be sold back to us. We must furthermore remember that we have issued more than $300,000,000 of additional emergency currency which gradually ought to be reduced.

The entirely unprecedented condition of the European markets will render advisable the greatest caution in dealing with our own. It is impossible at this time to foretell how long the disastrous wars will continue or to predict what will be the financial and commercial conditions when the day of final settlement will come. Our own country has been developed largely with the help of European capital and we have been accustomed annually to place in Europe hundreds of millions of dollars of securities. The old countries were glad to take

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these because the rates of interest offered by our investments were more attractive than those to be received from their own. It is impossible to predict what the ultimate effect will be, but it is to be apprehended that at the end of this war investment returns in Europe will be higher than they were in the past. The great destruction of property and the unparalleled expense to which those nations have been put will not only render their savings unavailable for our country but, instead of buying new securities from us, they may be willing to sell back to us securities now held on the other side. This tendency will be the stronger the lower our money rates will be and, inversely, it will be lessened if our interest rates and investment returns are fairly high.

The problem of the Federal Reserve Banks is then a two-fold one: on the one hand to grant credit facilities, particularly where the abnormal conditions now prevailing have created emergencies calling for prompt relief, and, on the other hand, to protect the gold holdings of this country and to enable it to stand all possible demands for gold to be made upon us by Europe. It would appear that this can best be done by supplying credit facilities liberally where there is a legitimate and urgent demand but at rates sufficiently high so as to reduce the pressure upon the Federal Reserve Banks and at the same time to discourage too large a back flow of securities to our shores. This policy must be adopted, not only by the Federal Reserve Banks, but also by the member banks which, when the new reserve requirements go into effect, should employ a substantial part of the amount of cash and reserve money set free in redeeming Aldrich-Vreeland currency and to increasing their cash balances with the Federal Reserve Banks.

While happily our international trade is improving by leaps and bounds and

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the hope appears to be well grounded that this country will turn in its favor the scales of the balance of trade, a period of conservatism and watchfulness is required until our new banking system will have been firmly established and until we can safely control the influences that may have an adverse effect on our own development. When this point is reached, the Federal Reserve Bank System will enable us to pass from a period of conservatism into one of conservative liberality in the granting of credit facilities.

The Federal Reserve Board, under Section 13 of the Federal Reserve Act, has the right to determine or define the character of "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."

Bearing in mind the requirements of the present situation, the Federal Reserve Board has reached the conclusion that it would be inadvisable at this time to issue any narrow regulation governing discount operations. It is from this point of view that it has been decided not now to enter upon the question of single or double name paper but to admit both forms of bills to rediscount with the Federal Reserve Banks. The Federal Reserve Board wishes, however, to establish the following rules and principles to be observed by Federal Reserve Banks and member banks.

Beginning by stating the case negatively, the rule is hereby established that, for rediscount with Federal Reserve Banks, no bill is to be admitted the proceeds of which have been or are to be applied to permanent investment.

It is the established principle of central banks to invest only in obligations maturing within a short time. The rule is generally observed not to

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purchase paper having more than ninety days to run; furthermore, that within these ninety days the maturities of these notes and bills should be so well distributed that it should be possible for these banks within a short time to increase their hold on the general money market by collecting at maturity, or reinvesting at an increased rate only, a very substantial portion of their bills owned. Acting on this theory, the Federal Reserve Banks should be able to practically liquidate whenever called upon to do so, one third of all their investments within thirty days. It is in following this principle that safety lies for the entire system and, at the same time, the justification for member banks to count balances with Federal Reserve Banks as a cash reserve. But safety not only requires that bills held by the Federal Reserve Banks should be of reasonably short and well scattered maturities, but in addition they ought to be of such character that, when they mature, it is certain that they can be collected. They ought to be (to use the term now so often applied) "self-liquidating". The basis of the bill drawn ought in every case to be some step in the march of goods from producer to consumer; or, to state it in another way, in the gradual process of distribution. The nearer this process reaches the final consumer the smaller will be the amount involved in each trahsaction as represented by the bill, and the more self liquidating will be its character. Double name paper drawn against the sale of goods on the purchaser is, from the economic point of view, the clearest evidence of the legitimate character of a bill. Single name notes, as used in our country, may represent the very same character of a transaction though the firm having sold the goods will sell its own note to finance collectively a number of sales of this kind. Inasmuch, however, as the single name paper does not show on its face the character of the

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transaction against which it has been issued - a serious defect in this form of paper - it is incumbent upon each Federal Reserve Bank to insist that the character of the business and the general status of the firm offering its paper should be closely investigated and that the discounting bank be assured that the single name paper has not been issued for investments of a permanent nature or of a longer duration than should be safely financed by the sale of ninety-day notes. Only careful scrutiny as to these characteristics would render it safe for the Federal Reserve Bank to consider such paper investment as self liquidating at maturity.

At this point we reach then the conclusion that bills, in order to be eligible for rediscount by Federal Reserve Banks, should not be drawn against permanent investments; they should be drawn against some temporary process in the general advance from producer to consumer; they should essentially be self liquidating, and a statement should have been given to the bank purchasing the paper. It is most desirable in the beginning of the operation of the banks to simplify matters as far as possible and it is, therefore, thought unnecessary to exact that a statement of condition should be attached to each bill when sold to the banks, nor is it thought necessary to embarrass the member banks by subjecting them to new regulations with which, at the time of opening of the Federal Reserve Banks, they cannot possibly comply since they own large amounts of paper purchased before these rules were established. The Federal Reserve Board, however, believes it safe and equitable to establish the rule that, at the expiration of forty-five days after the opening of the Federal Reserve Banks no paper shall be rediscounted by them that does not bear on its face the eviden

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that it is eligible for rediscount under the broad rules and definitions above outlined, and that the party selling the paper has given a statement to the member bank. A rubber stamp saying in substance:

Eligible for Rediscount with Federal Reserve Banks CREDIT FILE NO. .... DISTRICT NO. ..... (Name of Member Bank)

would be considered sufficient evidence to this effect. It would be understood that the Federal Reserve Bank could at any time call for this credit file and it may well be expected that these credit files, particularly of more important firms and of those rediscounting larger amounts, will be assembled in the Federal Reserve Banks and form the nucleus of a credit bureau which in turn eventually may lead to a central credit bureau. For the time being certified statements shall not be required, this is to be left open for further regulation at a later date. The statement should contain a short general description of the character of the business, balance sheet, profit and loss account. Assets should be divided into fixed investments, slow investments and quick investments; on the liability side should be shown capital, long time borrowing and borrowing on short term. Short term borrowings ought to correspond to quick assets and the statement should be convincing that short term paper is not being sold against permanent investments or slow assets. The statement should furthermore contain the maximum amount up to which the firm issuing this paper expects to borrow in the aggregate on short credit or sale of its paper, and the firm giving the statement should obligate itself to inform the bank and secure its consent before exceeding this limit. The affixing of the stamp stating such paper to be eligible for rediscount will be con-

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sidered as an affidavit by the member bank that the statement has been examined from this point of view and that the paper bought complies with the requirements as above outlined.

No Federal Reserve Bank should make any engagement with any member bank to renew paper at maturity at its then existing governing discount rate or otherwise, and it is urged that member banks abstain from pledging themselves to renew from their customers ninety day paper and thereby practically making it six months paper. It is apparent that, for certain branches of trade and manufacturing, it is impossible to liquidate a transaction within three months and that a credit of six months would be necessary to carry to its end either the process of production or manufacturing or the conclusion of the liquidation of the entire stock. While it is proper for borrowers to rely to a certain extent upon their ability to renew their paper, it would appear conservative that borrowers in need of a six months credit for the completion of their business should either be encouraged to provide a larger proportion of working capital of their own than those who are able to liquidate within a ninety day period or to force them not to carry too extensively their finished product. Producers forced by the nature of their business to renew their ninety day borrowings should be impressed with the fact that they are taking this risk. The banks should not take it for them and the more the period of temporary borrowing and production be brought into closer proportion the safer will be the entire banking system.

The law provides that the Federal Reserve Board shall fix the percentage of the capital (by which is understood capital paid in) up to which a Federal Reserve Bank may discount "notes, drafts, and bills drawn or issued for agricultural purposes or based on live stock and having a maturity not exceeding six

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months". The law gives latitude to the Federal Reserve Board to deal with each Federal Reserve Bank individually in fixing this limit. The Federal Reserve Board hereby fixes this limit generally, and until further notice, at twenty per centum of the capital paid in from time to time. For those districts in which, during certain seasons, six months paper is particularly required to carry through agricultural and farm operations, the limit will be increased from time to time. It would appear that, particularly in the cattle raising districts where the output is a continuous one it will not be difficult for the banks purchasing six months paper to scatter their maturities in such a way that a substantial amount of their paper could always have run off and be reduced to ninety day paper so as to give these banks a fairly continuous and ample supply of paper eligible for rediscount with the Federal Reserve Banks. In other districts, like the cotton growing ones, where requirements for six months paper are based on seasonal operations and therefore will be made upon the banks to a large extent at the same time, it is suggested that, as heretofore, these banks will find it convenient to place the most substantial part of their six months paper with other banks of the country and carry themselves a certain amount. The Federal Reserve Banks cannot, under the law, and should not for their protection and safety, invest beyond a certain limit in six months paper.

The law does not limit the aggregate amount of rediscounts to be granted by the Federal Reserve Banks to each member bank and the question has been raised as to whether any member bank should be entitled to send in for rediscount at the bank rate then governing any amount of paper, provided the quality of the paper would appear satisfactory to the Federal Reserve Bank. This ques-

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tion is to be answered in the negative. It is true that, on the one hand, it is the object of the law to make balances lying idle in one part of the country, or in one part of a district, or in any one bank, available for the other where bank accommodations may be legitimately required. But, on the other hand, it would be unfair to depositing banks not having called upon the Federal Reserve Banks for any rediscounts, to use their reserves to such a degree that their own legitimate demands could be met only upon more onerous terms because the weaker or less conservative banks would already have absorbed all the readily available credit. The policy of the entire system will have to be one of equalizing and guiding the ebb and flow of available resources, but until a free and country-wide discount market will have been established, which will be the most effective means of equalizing, it will be necessary for the directors of the Federal Reserve Banks to use their discretion in granting rediscounts. They will have to make careful examinations of their own status and that of the other Federal Reserve Banks and it will be their duty to form as accurate as possible a judgment as to the aggregate facilities which they can safely supply and to form an estimate of the probable demands and the directions whence they would be likely to come. After carefully weighing these two factors in the light of conditions existing in the other Federal Reserve Banks and reviewing the position of the entire country in its relation with the other nations of the world, they will have to reach conclusions as to what would be a fair share to be allotted to applying member banks. In the beginning it will be an extremely difficult task both for the directors and for the Federal Reserve Board on whom they will call for guidance. After a few years of actual experience and compiling of statistics showing to some extent the

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normal supply and demand of each district, the task will be much easier, and the further a free discount market develops the easier will be the means of handling the situation, but in starting a system entirely new to our country it will be necessary in many respects to feel our way carefully and learn by experience.

Bank Acceptances

The free use of American bank acceptances in financing transactions involving our imports and exports will be a great factor in establishing an American discount market. The American bank acceptance must become a popular investment all over the world. It must compete with those of England, Germany and France, and, in order to achieve this end, it must have a regular and reliable home market and the discount rate at which it can be placed must, as far as possible, meet that of the competing countries. This is all the more necessary as the bank acceptances of these other countries are well known all over the world and foreign nations are thoroughly familiar with the methods of disposing of these bank acceptances. A concerted effort will be necessary to establish a full and equal standing for the American bank acceptance in the world's market. It follows from this and other considerations (which it would lead too far to enlarge upon) that the discount rate for American bank acceptances must be lower than that for single name paper endorsed by member banks, and it will be, therefore, from the point of view of return, a poor investment for the Federal Reserve Banks. From the national point of view, however, it will be necessary that the question of return be disregarded by Federal Reserve Banks when acquiring bank acceptances. The larger question involved should be the guiding factor.

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The report by the Committee on Commercial Paper, approved by the conference of Federal Reserve Bank Directors at Washington on October 22, recommended that this question of bank acceptances be dealt with on a joint plan and for the joint account of the Federal Reserve Banks and that the Executive Council of Governors of the Federal Reserve Banks should, from time to time, regulate the method and the rates to govern the transactions in bank acceptances. It would appear as if it might be advisable to adopt a plan that these acceptances should be purchased for joint account, on a pro rata basis of capital or deposits, by those Federal Reserve Banks which, from time to time, have the lowest bank rate.

The Federal Reserve Board is in full accord with these recommendations and urges that prompt steps be taken by the Executive Council of Governors to establish a basis for dealing with bank acceptances.

Under Section 14 (d) power is given to the Federal Reserve Banks "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". This would permit the Federal Reserve Banks to establish different rates of discount for single name paper, for double name paper, for bank acceptances and different rates also for various maturities. It is natural that there should be a rate for six months paper different from that governing three months paper, and at times it may prove very advisable to have a different rate for thirty day paper from that for ninety day paper. From the point of view of a Federal Reserve Bank, desirous of securing the greatest possible liquidity, paper having to run not to exceed thirty days is a most

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desirable investment, and this in itself might warrant, at times, the lower rate. But, in addition, there is the further consideration that it is desirable to train the member banks to use less extensively the call loan market of the stock exchange as the means of equalizing daily balances, but rather to use their short paper for this purpose. It is, therefore, advisable to encourage the habit of even the strongest banks to rediscount their bills maturities when necessary for their daily requirements.

It appears advisable, however, to move slowly in this respect, and the suggestion is made at this time to serve as a topic for further careful consideration of the Executive Council of Governors.

P. H. W.
12-30-14

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14

WHEREAS, under Section 10 of the Act approved December 23, 1913, and known as the Federal Reserve Act, the Federal Reserve Board is empowered to levy semi-annually upon the Federal Reserve banks in proportion to their capital stock and surplus, an assessment sufficient to pay its estimated expenses including the salaries of its members, assistants, attorneys, experts and employees for the half year succeeding the levying of such assessment, together with any deficit carried forward from the preceding half year, and

WHEREAS, Under Section 16 of said Act, said assessment shall include a sufficient amount to cover expenses incurred in connection with the issue and redemption of Federal Reserve notes provided for in said Section, including cost of plates and dies to be engraved, the distinctive paper used and the cost of printing or engraving such notes, and

WHEREAS, It appears from estimates submitted and considered that it is necessary that a fund equal to _____ per cent of the capital stock of the Federal Reserve banks be created for the purposes hereinbefore described,

NOW, THEREFORE, BE IT RESOLVED, That pursuant to the authority vested in it by law, the Federal Reserve Board hereby levies an assessment upon the several Federal Reserve banks of an amount equal to _____ per cent of the capital stock of such banks, and the Secretary to the Board is hereby authorized to collect from said banks such assessment and execute in the name of this Board a receipt for payments made. Such assessment may be collected in three instalments of one-third each; the first instalment to be paid upon notice of the Secretary to such banks, the second instalment within thirty days and the third instalment within sixty days from said notice.

The foregoing is a true and correct copy of resolution duly offered and adopted by the Federal Reserve Board at a meeting held on _____day of November, 1914.

FEDERAL RESERVE BOARD,

By_____Acting Governor.

(SEAL)

ATTEST_____
Secretary.

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#34

15

ANNOUNCEMENT.

The Secretary of the Federal Reserve Board today sent to all Federal Reserve Banks copies of a resolution levying an assessment of four-tenths of one per cent against the several Federal Reserve Banks for the purpose of defraying the estimated total expenses in connection with the work of the Board. The assessment includes an estimated charge for the preparation of Federal Reserve notes and dies therefor of over $200,000. This item of cost will be very much less after the system has opened and the Federal Reserve Banks have been placed in operation. The actual cost of maintaining the Board cannot be figured with any degree of exactness owing to the circumstance that the number and extent of the Board's staff has yet to be determined. The first assessment is, therefore, based upon rough estimates of probable cost.

Federal Reserve Banks are requested to make remittance of one-third of the amount of their assessment immediately, a second third within thirty days, and the third installment within sixty days from date. The basis of estimate is the capital stock allotted to applying member banks figured at its full face value or about $110,000,000 for the whole system.

The actual assessment is intended to cover the outlay during the first half year.

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EXHIBIT B.

Chairman, Board of Directors
Federal Reserve Bank of_____,

_____.

S I R : -

For your information, please find enclosed certified copy of a resolution of the Federal Reserve Board levying an assessment of 4/10ths of one per cent against the several Federal Reserve banks for the purpose of defraying the estimated total expenses in connection with the work of this Board as prescribed in the Federal Reserve Act.

It is necessarily difficult to foretell the total expenses of every kind and nature incident to the development of the System, but the above assessment is believed to be sufficient to cover all expenses for a period of six months.

This assessment is based upon the capital stock of the several Federal Reserve banks, namely, an amount equal to six per cent of the aggregate total capital and surplus of all member banks.

In carrying out the requirements of the resolution above referred to, you are requested to make remittance of the first one-third of your share of this assessment at this time; a second installment of one-third within thirty days and a third installment of one-third within sixty days from this date.

In calculating your assessment you should take as a basis the capital stock allotted to the applying member banks by the Reserve Bank Organization Committee, as shown by the transcript of stock register furnished you for the purpose of opening your stock ledger.

Any discrepancy resulting from a decrease or increase of capital and surplus of member banks since the allotment was made by the Reserve Bank Organization Committee will be adjusted after your stock ledgers have been opened and checked. This adjustment may be deferred until the payment of the final installment, due sixty days from this date.

Remittances should be made in the form of check or draft payable to the "Federal Reserve Board."

Respectfully,

(Signed) H. Parker Willis,

Secretary.

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BIDS SENT IN BY BONDING COMPANIES

COMPANIES.	GOV. & BK. STF.	FED.RES. AGT. & STAFF	FED.RES. AGENT ALONE	DEP.FED RES.AGT	STAFF OF FED RES.AGT.
International Fidelity Ins. Co., #15 Exchange Place, Jersey City N. J.	$2.20		$1.00	$1.00	$2.20
American Fidelity Co., 9th & New York Avenue, Washington, D. C.	$2.00	$1.00 for each bond		$1.00 for ea. Bond	
American Indemnity Co., Galveston, Texas	$2.00	$1.00		$1.00	
(1) U. S. Fidelity & Guaranty Co. Baltimore, Md.	$2.50		$1.00	$1.00	$2.50
(2) U. S. Guaranty Co., 111 Broadway, N. Y.	$2500 to $25000 at $2.00	75% of rate for Gov & Staff	Reports will be made on officers & Staff of banks.		
New Amsterdam Casualty Co. Baltimore, Md.	$2.50		$1.00	$1.00	$2.50
Royal Indemnity Company 410 Bond Building, Wash. D.C.	$2.50	Blanket bond, same rate, liability to be ascertained by multiplying the penalty of the bond by the No. of exposures.	$1.00	$1.00	$2.50
Fidelity & Casualty Company, 520 Colorado Building, Wash., D. C.	$2.50	$1.00 Running to the Government $2.50 Running to the Banks.	$1.00 $2.50	$1.00 $2.50	$1.00 $2.50
Aetna Accident & Liability Co. Hartford, Conn.	$2.50		$1.00 Usual Govt. form of bond.	$1.00	$2.50 Honesty form of bond only
American Surety Company 100 Broadway, N. Y.	$2.50		$1.00	$1.00	$2.50
Hartford Accident & Indemnity Co. Hartford, Conn.	$2.50				
Southern Surety Company, 605 F Street, Washington, D.C.	$2.50		$1.00	$1.00	$2.50
Maryland Casualty Company, Baltimore, Md.	$1.00 for bonds running to the U. S. $2.50 for bonds running to the banks.				
Pennsylvania Surety Company, Baltimore, Md.	$2.50 Blanket bond $2.50 calculated by multiplying the penal sum by the individual covered.		$1.00	$1.00	$2.50
Chicago Bonding & Surety Co. 412 Fifth Street, Wash. D. C.	$2.50 Blanket bond $2.50 calculated by multiplying the penal sum by the individual covered.		$1.00	$1.00	$2.50
Massachusetts Bonding & Ins. Co. 77 State Street, Boston, Mass.	$2.50 Blanket bond $2,50 calculated by multiplying the penal sum by the individual Covered.		$1.00	$1.00	$2.50
Equitable Surety Co., St. Louis, Missouri	$2.50		$1.00	$1.00	$2.50

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Illionois Surety Company, 211 Colorado Building, Wash.,D.C.	$2.50			$1.00	$2.50
Casualty Company of America, 1500 Bond Building,Wash.,D. C.	$2.50		$1.00	$1.00	
Fidelity & Deposit Company, of Md. Baltimore, Md.	$2.50	$2.50		$2.50	
JOINT BID. National Surety Co.,115 Broadway,N.Y. Fidelity & Cas.,Co.,New York, N.Y. Globe Indemnity Co.,New York,N. Y. New England Cas.Co.,Boston, Mass	$2.50		$1.00	$1.00	$2.50

Bid may also be considered for each Company separately. Investigation of employees will be undertaken for Board or banks to a limited extent.

(1) "In addition to the above regular schedule bond or bonds we also offer to write the enclosed excess blanket fidelity bond, our bank form 91, for $50,000 in favor of each or any one of the Federal Reserve Banks on behalf of any twenty-five officers or employes in any one principal bank or in any one branch at a premium of $750.00 upon the condition that said twenty five officers or employes will be bonded under a schedule bond or under a primary coverage for amounts equal to the amounts outlined in schedule #2 on the reverse of said excess blanket bond. Provided also that the amounts for which said officers or employes are bonded to the Bank primarily either under a schedule or under separate bonds shall aggregate at least $200,000.00."

"If it is desired to have more than twenty-five officers or employes covered by this excess blanket bonds, we will add additional men to this excess bond at a premium of $15.00 per man, provided said parties are also primarily bonded to the Bank in accordance with schedule #2 on the roverse of said excess blanket bond."

"It is our opinion that it will be desirable to cover many of the minor clerks and employes only in comparatively small amounts. To cover such employes for $50,000. or $60,000. would obviously be to over-insure them. This protection may besecured by covering such employes under the schedule bond for the proper penalties and the twenty-five or more of the officers or directors in each principal bank or in each branch bank, who have access to large amounts, may be selected to be covered under the excess blanket bond of $50,000. in addition to the amounts for which they are covered under the regular schedule bond."

I

(2) "A schedule bond covering Governor and Staff individually for stated amounts varying from $2500 to $10,000 (or even up to $25,000) on each, according to responsibility of position held, at a premium rate of 20 cents per $100. per annum as a primary coverage."

"Excess loss over such primary coverage to be covered by a policy or policies in blanket form issued by other company, or companies for amounts desired, say $100,000. to $250.000. according to size of Bank, (Rate on such excess coverage should be very moderate)."

2.

"A bond in blanket form on Governor and Staff Collectively covering loss up to $25,000 through any one or more or all persons named in the schedule forming part of the bond, to be held as a primary coverage, at annual rates as follows:-

1st 100 names	@ $20.00 each	2000.00
2nd 100 "	" 12.50 "	1250.00
3rd 100 "	" 7.50 "	750.00
4th 100 "	" 5.00 "	500.00
400	" (averaging $11.25 each	$4500.00

Each additional name (beyond 400) each $4.00

"Excess loss over such primary coverage to be covered by a policy or policies in blanket form issued by other company or companies for amounts desired, say $100,000 to $250,000 according to size of Bank.(Rate on such excess coverage should be still lower than on exce under No. 1. because of the higher primary coverage".

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STATEMENT FOR THE PRESS.

Payment of the first installment of the capital stock of Federal Reserve Banks, called for on November 2nd, has been practically completed.

The amounts paid in, as reported to the Federal Reserve Board today, are as follows:

Boston	$1,617,925.
New York	3,320,380.10
Philadelphia	2,068,559.41
Cleveland	2,012,353.80
Richmond	1,063,458.55
Atlanta	777,248.63
Chicago	2,191,000.
St. Louis	912,000.
Minneapolis	794,500.
Kansas City	916,000.
Dallas	951,335.
San Francisco	1,322,346.24
	$17,947,106.73

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The Governors of the Federal Reserve Banks.

Gentlemen:

I submit a statement with reference to the work placed in my charge relating to accounting systems for use in Federal Reserve Banks and equipment therefor. Such assignment having been made partly by the Organization Committee of the Federal Reserve Board, partly by the Convention of Directors which met in Washington October 22nd, and partly by several of the Governors of the banks acting together on a later date.

In January 1914, I was requested by the Secretary of the Treasury, as Chairman of the Organization Committee, to form a preliminary committee of experts for the purpose of considering questions respecting the organization of Federal Reserve Banks. This duty was carried out and part of the work of the Preliminary Organization Committee thus formed by me consisted in preparing accounting plans for the banks. With expert assistance, two such plans were formulated and were presented to the Board. Both were referred by the Board to the Bureau of Efficiency, U. S. Civil Service Commission, which, after examination of both plans, reported in favor of a system prepared under the direction of Messrs. Harry E. Ward and C. C. Robinson, of New York City, acting as expert advisers to the sub-committee on mechanical accounting which had been appointed by the Preliminary Organization Committee already described and of which I was Chairman. Subsequently the two systems already mentioned were referred by the Board to Mr. W. P. G. Harding, one of the members of the Board, as a sub-committee. Mr. Harding carefully discussed both systems with me and finally presented to the Board a report coinciding with that of the Bureau of Efficiency. This report was adopted by the Board. At the convention of Directors and officers of Federal Reserve Banks held in this city on October 20-22 a sub-committee of the convention to deal with statistics and accounting was appointed.

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This committee devoted two days' work o consideration of both the accounting systems, whose genesis has already been described and reported back to the convention favorably the same system that had already been approved by the Bureau of Efficiency and by Mr. Harding and-by the Board itself. A report of this committee is embodied in circular No. 11 issued by the Board, which includes the reports of committees to the convention. A copy of circular No. 11 is attached hereto as Exhibit A. In adopting the report thus laid before it, the convention, however, expressly requested that the Board should refer the accounting system to a meeting of Governors to be held after the close of the convention. This meeting was held on October 22nd, and there were present: Mr. Theodore Wold, Governor of Federal Reserve Bank of Minneapolis, Mr. George J. Seay, Governor, Federal Reserve Bank of Richmond, Mr. Archibald Kains, Governor, Federal Reserve Bank of San Francisco, Mr. Alfred L. Aiken, Governor, Federal Reserve Bank of Boston, Mr. Charles M. Sawyer, Governor, Federal Reserve Bank of Kansas City, Mr. Joseph A. McCord, Governor, Federal Reserve Bank of Atlanta, Mr. Oscar Wells, Governor, Federal Reserve Bank of Dallas.

Governor Benjamin Strong, Jr., Federal Reserve Bank of New York City, had already, on a previous occasion, devoted careful study to the accounting system and had approved it. Governor James B. McDougal, Federal Reserve Bank of Chicago, and Governor Rolla Wells, Federal Reserve Bank of St. Louis, had not at that time been elected, while Governor Charles J. Rhoads, of the Federal Reserve Bank of Philadelphia, and Governor E. R. Fancher, of the Federal Reserve Bank of Cleveland, were not present. Federal Reserve Agent D. C. Wills, of Cleveland, had, however, been a member of the Committee on accounting and had devoted very careful attention to the whole subject on a previous occasion. The seven Governors who were present on October 22nd carefully reviewed the system of accounting in conjunction with Mr. C. C. Robinson, who had been largely instrumental in framing it, and with myself. At the conclusion of their investigation the scheme of accounting was tentatively approved by them subject to further investigation on their return home, and the following requests

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were made of me:

1. To place contracts for printing the accounting forms embodied in the system; to receive orders from such of the banks as might choose to introduce them, and to distribute the forms in accordance with such orders.

2. To obtain bids for machines suitable for use in equipping the banks to carry bookkeeping operations involving the use of the proposed accounting system; to classify such bids; and to inform the several banks of the result in order that they might, in their discretion, supply themselves with machine equipment.

Subsequently three of the banks requested me to place their actual orders for machines in accordance with the decision that might be arrived at after bids had been obtained and opened.

In accordance with the request thus made to me, I at once proceeded to place the contract for the accounting forms, having obtained the services of Mr. C. C. Robinson as consulting expert to aid in this and other allied work. Recognizing that the time would be extremely short before the opening of the banks, I had already obtained bids from several responsible concerns for the printing of the forms in order that if they should be adopted there might be no delay in beginning operations. It had been found when these bids were opened that most of the proposals were incomplete, owing to the fact that few concerns were equipped to handle so large an undertaking. Of the few complete proposals, that of the Westside Printing Company of New York City, was the lowest. It was also found that most of the printing concerns asked from 60 to 90 days to complete the work, while the Westside Printing Company undertook to do it in less than 30 days. The Government Printing Office asked 60 to 90 days for the preparation of the forms. Inquiry of other concerns produced the reply that the work could not be furnished in less than 20 days even with the utmost effort. In order to facilitate matters it was determined to ask a number of responsible firms if they would take a part of the work at the figures fixed by the Westside Printing Company's bid

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This proposal was accepted by the Falconer Company, of Baltimore and Foote and Davies Company, of Atlanta, Ga. The Westside Printing Company found four other concerns in New York who were willing to accept a portion of the order on the proposed basis. The order was accordingly divided between the Westside Printing Company, The Falconer Company, Foote & Davies Company, and the sub-contractors already referred to. The contracts were placed on the 23rd of October and delivery began within about a week thereafter. By November 4th all the orders had been completed and shipped. It was determined that in order to prevent delay a minimum supply of forms should be shipped by express to each bank, the balance of the order to follow by freight, that the preliminary shipments should be equipped with binders and that a supply of carbon paper adequate to start the banks in the use of the forms upon the 16th of November, pending such time as they could supply themselves more fully, should be furnished. The printers were ordered to furnish those binders which in their opinion were most suitable for the purpose and to add the cost to their statement.

There is submitted herewith as exhibit B the complete detailed bid of the Westside Printing Company which was used as a basis on which the assignment of the work to the different concerns was made.

With reference to the second matter entrusted to me - the selection of machines - the method adopted was as follows: I first formed a committee to deal with the matter, consisting of Mr. Sherman P. Allen, Assistant Secretary, Federal Reserve Board, Mr. Charles A. Kram, Mr. C. C. Robinson, Mr. Howard R. Barnes, and myself, and as the time available was more adequate than in the case of the accounting forms, advertisements were placed in newspapers in the following cities: Washington, New York, Boston, Chicago.

The advertisement read as follows:

> "Bids will be received in the office of the Secretary of the Federal Reserve Board, Treasury Department, Washington, D. C. for typewriters, adding machines, and other labor-saving devices to be used in the twelve Federal Reserve Banks on October 31st,1914. Demonstrations of machines, may be arranged by applying to H. P. Willis, Secretary".

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Bidders immediately began to file their proposals and to ask for demonstrations. Every such request for demonstration was honored and an examination of the various mechanisms was made by some one or more members of the Committee. Bids were closed on October 31st, and on November 2nd a meeting of the Committee attended by Mr. Sherman P. Allen, Mr. C. C. Robinson, Mr. Charles A. Kram, and myself, was held in the office of the Secretary of the Federal Reserve Board. At this meeting the bids were opened and classified, and the following notes of proceedings were made during the meeting:

"The Committee decided to establish a classification of bids too incomplete to receive consideration."

"The Committee made note of the fact that as binders have been supplied by the printers it was not necessary to include consideration of binder bids in the report."

"The Committee determined to consider no bids for letterheads or plain stationery, etc., considering that to be outside of its function."

"The Committee determined to establish a separate classification for adding typewriters."

"The Committee established a classification to which were assigned all straight adding machines without typewriter attachment."

"The Committee determined to establish a separate classification for filing devices."

"The Committee determined to establish a classification to which were assigned bids for calculating machines."

"The Committee determined to establish a list of machines whose use would be entirely optional with the individual banks as a basis for checking and incidental adding."

"The Committee established a separate classification for standard typewriter bids."

Mr. Charles A. Kram and Mr. C. C. Robinson were then appointed a committee to consider the bids more in detail and to prepare a classified list of bids, grouping the devices as applicable to the various departments of the banks as required by the accounting scheme already adopted. This sub-committee presented to the full committee a report embodying the classification of bids to which I have referred

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This report of the sub-committee was at once mailed to all Governors in order that they might have it available. A copy of it is annexed hereto as exhibit C.

Upon further consideration it was deemed wise to invite to Washington the accounting officers of the several banks for the purpose of further explaining to them the accounting system and of enabling them to buy without further delay the machines needed. Invitations were accordingly sent out by telegraph for a meeting on November 2nd and at the same time manufacturers were informed that if they desired,a room would be placed at their disposal in the Treasury Building for the purpose of demonstrating their machines. Many of them availed themselves of this invitation and in consequence an exhibit of about twenty-eight machines and devices was assembled in Room 28 of the Treasury Building.

On November 2nd there met at the Treasury Department representatives of the Federal Reserve Banks of Boston, New York, Philadelphia, Cleveland, Richmond, St. Louis, Kansas City, and San Francisco. The following banks were not represented: Minneapolis, Chicago, Dallas, and Atlanta.

The representatives of the eight banks referred to assembled in the Board Room and devoted two days to the accounting system in its practical aspects and to the testing of the various machines on the accounting forms, the forms being run through the various machines. As a result, several placed orders for the machine equipment then deemed necessary, while others prepared memoranda as to their requirements, such memoranda to guide them on their arrival at their several institutions. As I had myself been requested by three banks to place their orders, I did so; being guided by the following considerations in selection:

a. All machines selected were those which had been proved practically efficient by actual tests made in my presence.

b. The combined cost of the machines selected was as low as the competitive bids would permit.

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c. The machines selected were to be those whose manufacturers were prepared to guarantee the smooth working of the machines when installed and who were in position to oversee them from their local offices. Bearing this point in mind, I placed orders as follows:

For the Federal Reserve Bank of Richmond:

Copy of Machine Equipment arranged for
the Federal Reserve Bank of Richmond, Va.

Transit Department:

Two Ellis Machines - Total cost.....$550.00

Bookkeeping Department:

Two Remington, "B" carriage, Standard typewriters, with cross and vertical adding and subtracting actuator, capacity 999,999,999.99, with four eleven wheel totalizers - Total cost.....$1,127.00

Discount Department:

One Remington Standard Duplex -Price... $810.00

Federal Reserve Agent:

Remington, #10-D Carriage,
Elite type - Price..... $80.50

Ordinary Typewriters:

Four L. C. Smiths,10" Carriage
Total cost $260.00

Three Underwoods, Model H-5, 10"
Carriage - Total cost 210.00

Adding Machines:

Five Burroughs Adding Machines,
9 Bank, Model 126, Hand Power - Total Cost.....$1,487.50

$4,525.00

Remington Typewriter Company:

The machines of the Remington Company have been ordered for your use under a sixty day option, which will permit you to definitely determine their adaptability to your forms, it being understood that at the end of this sixty day period, should any or all of the machines be purchased, bills covering such purchases are to be forwarded to you and will contain the clause "Cash within thirty days from date of invoice, net".

??"""""""# The Remington Company also agrees to forward two additional machines of this type for your temporary use, and in the event of your desiring to retain them, their subsequent purchase will be made exactly in accordance with the specifications in the above paragraph.

Burroughs Adding Machine Company:

In addition to the five Burroughs Adding Machines as outlined above, it is understood that five additional machines of the same model will also be delivered, such machines to be considered as having been borrowed for a period of, say sixty days, at the expiration of which time, should you desire to purchase all or a portion thereof, they are to be billed to you, such bills to contain the clause "Cash within thirty days from date of invoice, net".

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Ordinary Typewriters:

The typewriters purchased from the John Underwood Company and L. C. Smith & Bros. Typewriter Company are not to be billed to you until on or after December 1, 1914.

All of the above equipment call for delivery in your hands no later than November 12, 1914.

??"""""""# Model #11 "B" Cross Adder. Bookkeeping Dept.

- - - - - - -

For the Federal Reserve Bank of San Francisco:

Copy of Machine Equipment arranged for the Federal Reserve Bank of San Francisco, California.

Transit Department:	
Two Remington Standard Typewriters, with automatic feed roll release, short holding bale, "C" carriage - Total cost.....	$269.50
Bookkeeping Department:	
Two Remington, "B" carriage, Standard typewriters, with cross and vertical adding and subtracting actuator, capacity 999,999,999.99, with four eleven wheel totalizers - Total cost.....	$1,127.00
Discount Department:	
One Remington Standard Duplex, Price.....	$810.00
Mail Department:	
One Montague Addressing Machine, Type "N", motor driven, with ten cold rolled steel filing drawers - Price.....	$155.00
Federal Reserve Agent:	
Remington, #10-D Carriage, Elite type - Price	$80.50
Ordinary Typewriters:	
Four L. C. Smiths, 10" carriage - Total cost.....	$260.00
Three Underwoods, Model H-5, 10" carriage - Total cost	210.00
Adding Machines:	
Five Burroughs Adding Machines, 9 Bank, Model 126, Hand power - Total cost.....	$1,487.50
	$4,399.50

Remington Typewriter Company:

The machines of the Remington Company have been ordered for your use under a sixty day option, which will permit you to definitely determine their adaptability to your forms, it being understood that at the end of this sixty day period, should any or all of the machines be purchased, bills covering such purchases are to be forwarded to you and will contain the clause "Cash within thirty days from date of invoice, net".

??"""""""""""# The Remington Company also agrees to forward two additional machines of this type for your temporary use, and in the event of your desiring to retain them their subsequent purchase will be made exactly in accordance with the specifications in the above paragraph.

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Burroughs Adding Machine Company:

In addition to the five Burroughs Adding Machines as outlined above, it is understood that five additional machines of the same model will also be delivered, such machines to be considered as having been borrowed for a period of, say, sixty days, at the expiration of which time, should you desire to purchase all or a portion thereof, they are to be billed to you, such bills to contain the clause "Cash within thirty days from date of invoice, net".

Montague Mailing Machinery Company:

This machine likewise will be delivered under a sixty day option as specified for the Remington Typewriter Company. It will be forwarded to you by freight, and in the meanwhile the necessary plates will go forward to the San Francisco office by express, upon receipt of which a temporary machine, together with the plates, will be delivered to you on or before November 12, 1914. This machine, of course, will be substituted by that now being forwarded by freight.

Ordinary Typewriters:

The typewriters purchased from the John Underwood Company and L. C. Smith & Bros. Typewriter Company are not to be billed to you until on or after December 1, 1914.

??"""""""""# This covers two additional machines for the Bookkeeping Dept.

With the exception of the Montague machine arrangements for all of the above equipment call for delivery in your hands no later than November 12, 1914.

For the Federal Reserve Bank of Dallas:

Copy of Machine Equipment arranged for
The Federal Reserve Bank of Dallas,
Texas.

Transit Department:

Two Remington Standard Typewriters, with automatic feed roll release, short holding bale, "C" carriage - Total cost $269.50

Bookkeeping Department:

Two Remington "B" carriage, Standard typewriters, with cross and vertical adding and subtracting actuator, capacity 999,999,999.99, with four eleven wheel totalizers - Total cost $1,127.00

Discount Department:

One Remington Standard Duplex, Price..... $810.00

Mail Department:

One Montague Addressing Machine, Type "N", motor driven, with ten cold rolled steel filing drawers - Price..... $155.00

Federal Reserve Agent:

Remington, #10-D Carriage, Elite type - Price..... $80.50

Ordinary Typewriters:

Four L. C. Smiths, 10" carriage Total cost $260.00

Three Underwoods, Model H-5, 10" carriage - Total cost $210.00

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Adding Machines:

Five Burroughs Adding Machines,
9 Bank, Model 126, Hand Power, Total cost $1,487.50
$4,399.50

Remington Typewriter Company:

The machines of the Remington Company have been ordered for your use under a sixty day option, which will permit you to definitely determine their adaptability to your forms, it being understood that at the end of this sixty day period, should any or all of the machines be purchased, bills covering such purchases are to be forwarded to you and will contain the clause "Cash within thirty days from date of invoice, net".

Burroughs Adding Machine Company:

In addition to the five Burroughs Adding Machines as outlined above, it is understood that five additional machines of the same model will also be delivered, such machines to be considered as having been borrowed for a period of, say, sixty days, at the expiration of which time, should you desire to purchase all or a portion thereof, they are to be billed to you, such bills to contain the clause "Cash within thirty days from date of invoice, net".

Montague Mailing Machinery Company:

This machine likewise will be delivered under a sixty day option, as specified for the Remington Typewriter Company. It will be forwarded to you by express, plates going under separate cover and will be delivered to you on or before November 12th, 1914.

Ordinary Typewriters:

The typewriters purchased from the John Underwood Company and L. C. Smith & Bros. Typewriter Company are not to be billed to you until on or after December 1, 1914.

Remington Typewriters Company #2.

The Remington Company also agrees to forward two additional machines for your temporary use in the Bookkeeping Department, and in the event of your desiring to retain them, their subsequent purchase will be made exactly in accordance with the specifications in the above paragraph.

At the same time, as I had been requested to do, I telegraphed to those banks not represented at the accounting sessions recommendations as to minimum outfit in order that they might, if they chose, avail themselves of the work which had been done.

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The following telegrams were sent to the Federal Reserve Bank of Chicago and Minneapolis:

TREASURY DEPARTMENT TELEGRAM.

November 5, 1914.

Federal Reserve Board

Mr. Theodore Wold, Governor,
Federal Reserve Bank,
Minneapolis, Minn.

Mr. James B. McDougal, Governor,
Federal Reserve Bank,
Chicago, Ill.

Mailed you last night list of compiled results of bids on machines and equipment. In accordance with request of governors now recommend following equipment as own personal judgment regarding minimum outfit to go with accounting system: Machines for transit, bookkeeping, discount and Federal Reserve agent departments and straight adding machines can be had from makers under arrangement offered by them on sixty days trial subject to return if found unsatisfactory with forms.

Transit Department: Two Ellis machines total cost $550.

Bookkeeping Department, Two Remington "B" carriage, standard typewriters, with cross and vertical adding and subtracting actuator, capacity 999,999,999.99 with four extra eleven wheel totalizers, total cost $1127.

Discount Department: One Remington Standard duplex price $1810.00.

Mail department, one Montague addressing machine, type "N" motor driven with ten cold rolled steel filing drawers, price $155.

Federal reserve agent, Remington #10-D carriage elite type price $80.50.

Ordinary typewriters, four L. C. Smiths 10" carriage total cost $260.00
Three Underwoods, Model H-5 10" carriage, total cost $210.00.

Adding machines, Five Burroughs adding machines nine bank model 126 hand power total cost $1,487.50

H. Parker Willis,
Secretary.

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The following telegrams were sent to the Federal Reserve Bank of Dallas and Atlanta:

TREASURY DEPARTMENT TELEGRAM.

November 5, 1914.

Federal Reserve Board

Mr. J. A. McCord, Governor,
Federal Reserve Bank
Atlanta, Ga.

Mr. Oscar Wells, Governor,
Federal Reserve Bank,
Dallas, Texas.

"Mailed you last night list of compiled results of bids on machines and equipment in accordance with request of Governors now recommend following equipment as own personal judgment regarding minimum outfit to go with accounting system. Machines for transit, bookkeeping, discount and Federal Reserve Agent department and straight adding machines can be had from makers under arrangement offered by them on sixty days trial subject to return if found unsatisfactory with forms.

Transit Department: Two Remington Standard typewriters with automatic feed roll release, short holding bale, "C" Carriage, total cost $269.50.

Bookkeeping Department: Two Remington "B" Carriage, standard typewriters with cross and vertical adding and subtracting actuator, capacity 999,999,999.99 with four extra eleven wheel totalizers. Total cost $1127.

Discount Department: One Remington standard duplex price $810.

Mail Department: One Montague addressing machine, type "N", motor driven, with ten cold rolled steel filing drawers, total cost $155.

Federal Reserve Agent, Remington No. 10D carriage, elite type, price $80.50.

Ordinary typewriters, four L. C. Smiths 10" carriage price $260.00
Three Underwoods, Model H-5, 10" carriage, total cost $210.00.

Adding machines 5 Burroughs adding machines 9 bank model 126 hand power total cost $1,487.50."

H. Parker Willis,
Secretary.

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As orders had been placed for three banks, six had been represented at the conference and the others notified. The results of the investigation have thus been made available to all the institutions in question.

Some bids which were received after the date set for closing the bids owing to lack of information on the part of the bidders were separately tabulated and transmitted as a supplementary list to all Governors.

I desire at this point to make acknowledgment of the assistance rendered by the special committee which considered the machine bids, and of the able work of Mr. C. C. Robinson in assisting me to carry through the requests of the Governors of the Federal Reserve Banks. Without his aid it would have been impossible to finish this duty in the time available for it.

This report closes the work undertaken by me at the request of the Governors for the purpose of aiding in the prompt installment of the accounting and machine systems in the several banks.

Respectfully submitted,

November 10, 1914.

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EXHIBIT B.

WEST SIDE PRINTING & SUPPLY CO.

Stationers & Printers

17 Murray Street

New York, October 16,1914.

Mr. H. Parker Willis, Sec.,

Federal Reserve Board,

Treasury Building,

Washington, D. C.

Dear Sir:-

We take pleasure in submitting herewith our estimate on forms for the Federal Reserve Bank system, tabulated as requested.

We might say in connection therewith that the greatest proportion of the forms submitted are of a character with which we are especially familiar, and we feel that should we be favored with your order, we are in the best position to give you the prompt service demanded.

We have endeavored, even while figuring, to so line up the required paper that we will be able to make the ten day delivery without trouble. We would especially urge that you notify us in the quickest possible time, as it may enable us to deliver prior to the ten day period.

Very truly yours,

West Side Printing & Supply Co.

(Signed) Robt. A. Snyder,

Pres.

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S P E C I F I C A T I O N S .

No. 1	Cost of setting type and furnishing proofs	$725.00
No. 2	Estimate to furnish forms for one bank	6,429.57
No. 3	Estimate for furnishing forms for one bank (Contingent upon receiving orders) (from all twelve banks)	4,750.00
No. 4	Above prices cover delivery under normal conditions	
No. 5	Estimates for furnishing forms for one bank (Contingent upon receiving orders) (from all twelve banks) under a 10 day dely.	5,250.00
No. 6	Estimates for furnishing forms for one bank (Contingent upon receiving orders) (from all twelve banks)under a 15 day dely.	5,050.00
No. 7	Estimates for furnishing forms for one bank (Contingent upon receiving orders) (from all twelve banks) under a 20 day dely.	4,950.00

WEST SIDE PRINTING & SUPPLY COMPANY

17 Murray Street,

New York City, N. Y.

(Signed) Robt. A. Snyder.

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DISTRIBUTING DESK

D. D. 1	6,000	$32.46	
D. D. 2	6,000	42.90	
D. D. 3	160	13.70	
			$89.06

SECURITIES

S. 1	1,000	$27.60	
S. 2	500	8.05	
S. 3	500	15.75	
S. 4	500	10.95	
S. 5	200	7.80	
S. 6	60	3.45	
S. 7	100	8.00	
			$81.60

MISCELLANEOUS

Misc. 1	18 Books	$150.00	
Misc. 2	5,000	10.00	
Misc. 3	5,000	8.00	
Misc. 4	500	2.50	
Misc. 5	500 Sets	5.00	
Misc. 6	500 Sets	4.50	
Misc. 7	200	11.85	
Misc. 8	200	6.05	
Misc. 9	2,000	6.00	
Misc. 10	2,000	10.00	
Misc. 11	50 Books	26.40	
Misc. 12	2,000	7.50	
Misc. 13	500	2.85	
			$250.65

AUDITING

A. 1	200	$4.40	
A. 2	1,000	4.00	
A. 3	4,000	30.00	
A. 4	4,000	10.75	
A. 5	600	3.50	
A. 6	2,000	4.00	
A. 7	500	7.50	
A. 8	500	28.44	
A. 9	200	4.85	
A. 10	160	12.50	
A. 11	3,000	11.85	
A. 12	50	35	
A. 13	2,000	3.25	
A. 14	100	4.15	
			$129.54

Forward $550.85

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		Brought forward	$550.85
RECEIVING TELLER			
R. T. 1	1,000	$14.85	
R. T. 2-6	2,500 each	8.60	
R. T. 7	2,000	15.30	
R. T. 8	160	10.00	
			48.75
MAIL TELLER			
M. T. 1	8,000	$36.05	
M. T. 2-4	7,500 each	6.60	
M. T. 5	160	12.50	
M. T. 6	5,000	34.00	
			89.15
TRANSIT			
T. 3	3,000	$31.70	
T. 4	3,000	24.90	
T. 5	50,000	264.25	
T. 6	50,000	208.50	
T. 7	4,000	57.45	
T. 8	1,000	10.10	
T. 9	3,000	17.50	
T. 10	1,000	3.45	
T. 11	1,000	4.60	
T. 12	2,000	21.00	
T. 14-16	3,000 each	8.08	
T. 17	8,000	38.25	
T. 18	160	12.50	
			702.28
FEDERAL RESERVE AGENT			
F. R. A. 1	1,000	$35.20	
F. R. A. 2	500	37.62	
F. R. A. 3	500	37.62	
F. R. A. 4	500	15.66	
F. R. A. 5	500 sets	11.75	
			137.85
BOOKKEEPING			
B. 1	50,000	$410.40	
B. 2	500	3.00	
B. 3	500	2.60	
B. 4	500	4.90	
			420.90
			$1,949.78

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		Brought forward		$1,949.78
DISCOUNT				
B. D. 1	1,000		$10.50	
B. D. 2	4,000		273.85	
B. D. 3	3,000		326.42	
B. D. 4	500		9.12	
B. D. 5	3,000		155.05	
B. D. 6	3,000		222.21	
B. D. 7	500		9.42	
B. D. 8	500		21.76	
B. D. 9	100		5.86	
B. D. 10	144		12.57	
B. D. 11	1,000		108.34	
B. D. 12	500		8.90	
B. D. 13	500		5.30	
B. D. 14	500		6.65	
B. D. 15	500		64.38	
B. D. 16	500		73.06	
B. D. 17	500		106.36	
B. D. 18	500		7.50	
B. D. 19	100		5.80	
B. D. 20	2,000		97.80	
B. D. 21	500	sets	18.35	
B. D. 22	500		20.37	
B. D. 23	2,000		38.46	
B. D. 24	1,000		8.15	
B. D. 25-26	2,000	each	6.00	
B. D. 27	160		8.00	
B. D. 28	500	sets	20.79	$1,651.00
CLEARING HOUSE				
C. H. 1	7,000		$35.76	
C. H. 2-5	6,000	each	12.90	
C. H. 6	160		12.50	
C. H. 7	4,000		23.80	
C. H. 8	160		12.50	
C. H. 9	5,000		34.00	
				131.46
ACCOUNTING				
A. C. 1	500		$11.25	
A. C. 2	1,000		14.17	
A. C. 3	500		11.24	
A. C. 4	500		33.70	
A. C. 5	1,000		32.00	
A. C. 6	500		17.96	
A. C. 7	1,000	sets	9.80	
A. C. 8	11	books	53.80	
A. C. 9	1,000		23.60	
A. C. 10	100		5.46	
A. C. 11	1,000	sets	21.84	
A. C. 12	1,000		7.60	
A. C. 13-16	2,500	each	7.50	
A. C. 17	160		10.00	
A. C. 18	500		3.80	
				263.72
				$3,995.96

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			Brought forward	$3,995.96

NOTE TELLER

N. T. 1	3,000		$18.60	
N. T. 2	500		13.30	
N. T. 3-7	12,500	Assorted	8.75	
N. T. 8	1,000	Separate	35.10	
N. T. 9	500		2.50	
N. T. 10	160		12.50	
				90.75

GENERAL BOOKKEEPER

General Ledger			$35.50	
G. B. 2	1,000		26.35	
G. B. 3	1	Book	10.50	
G. B. 4	300		3.50	
G. B. 5	1	Book	10.20	
G. B. 6	500		10.30	
G. B. 7	1	Book	20.70	
				119.05

COLLECTION

Coll. 1	3,000		$86.00	
Coll. 2	3,000		103.20	
Coll. 3	4,000		62.35	
Coll. 4	4,000		127.50	
Coll. 5	2,000		21.00	
Coll. 6	1,500		17.50	
Coll. 7	2,000		38.85	
Coll. 8	2,000		21.50	
Coll. 9	1,000		8.85	
Coll. 10	1,500		6.90	
Coll. 11	1,000		12.40	
Coll. 12-13	5,000	Assorted	4.15	
Coll. 14	160		12.50	
				522.70

PAYING TELLER

P. T. 1	2,000		$79.40	
P. T. 2	500		32.10	
P. T. 3	1,000		34.65	
P. T. 4	500		25.15	
P. T. 5	2,000		9.00	
P. T. 6	1,000		4.30	
P. T. 7	1,000		4.30	
P. T. 8	1,000		6.10	
P. T. 9-13	12,500	Assorted	8.00	
P. T. 14	160		12.50	
P. T. 15	500		24.35	
P. T. 16	200		2.20	
P. T. 17			6.00	
				248.05
				$4,976.51

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Brought forward $4,976.51

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FOREIGN EXCHANGE

F. X. 1	2,500 Sets	$130.69	
F. X. 2	2,000 Sets	117.40	
F. X. 3	500	40.50	
F. X. 7	2,000 Sets	209.90	
F. X. 8	1,500 Sets	194.82	
F. X. 9	1,500 Sets	173.76	
F. X. 13	500	18.60	
F. X. 14	500	18.60	
F. X. 15	2,500	36.75	
F. X. 16	2,500	8.75	
F. X. 17	500	7.30	
F. X. 19	500 Sets	6.90	
F. X. 18	300	7.02	
F. X. 20	500	2.34	
F. X. 22	200 Sets	9.95	
F. X. 23	200	5.90	
F. X. 25	1,000 Sets	5.25	
F. X. 26	500 Sets	10.00	
F. X. 27	200 Sets	6.00	
F. X. 29	300 Sets	4.50	
F. X. 30	1,000	17.60	
F. X. 31	500	12.26	
F. X. 32	500	12.26	
F. X. 33	2,500 each	6.30	
F. X. 34	2,000	17.35	
F. X. 35	500	19.10	
F. X. 36	300	20.40	
F. X. 37	200	6.50	
F. X. 38	200	6.50	
F. X. 39	300	8.16	
F. X. 40	200	7.40	
F. X. 41	1,500	13.40	
F. X. 42	200	3.40	
F. X. 43	200	3.40	
F. X. 44	1,000	10.50	
F. X. 45	1,000 Sets	8.22	
F. X. 46	1 Book	17.36	
F. X. 47	1,500	106.02	
F. X. 49	1,000	41.45	
F. X. 50	1,000	41.15	
F. X. 51	1,000	38.40	
F. X. 52	160	10.00	1,442.06

Gold Reserve Statement Book 11.00

Total..... $6,429.57

EXHIBIT "C" Previously Mailed.

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November 12, 1914.

STATEMENT FOR THE PRESS.

---oOo---

The applications of Charleston, South Carolina and Birmingham, Alabama to be made reserve cities, were favorably acted upon by the Federal Reserve Board today. Charleston was formerly designated as a reserve city in the National Bank Act.

The applications of Tulsa, Oklahoma, with 18,000 inhabitants, and Joplin, Missouri, with 32,000 inhabitants, census of 1910, were before the Board but did not receive favorable action.

It is understood that in the future no cities with less than 100,000 inhabitants will be approved as reserve cities.

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QUESTIONS SUBMITTED BY GOVERNOR AIKEN OF THE BOSTON FEDERAL RESERVE BANK WITH ANSWERS.

---ooOo---

1. Section 16, Federal Reserve Notes.

(a) Is it mandatory that the Federal Reserve Board shall establish a rate of interest to be charged upon Federal reserve notes issued, or is it optional?

Answer: It is optional.

(b) When such notes have been returned to Federal Reserve bank through which issued are they necessarily at once to be delivered to the Federal reserve agent for cancellation?

Answer: No. The bank could keep them in its cash.

2. Can Federal Reserve notes be issued to the Federal reserve bank except on application from member banks for rediscount and for notes as the proceeds of such rediscounts?

Answer: The reserve banks upon authority from the Federal Reserve Board can take out reserve notes, provided they deposit the commercial paper necessary as collateral on their own volition, without any prior application from member banks.

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3. On November 16th, will the Boston Bank be in a position to supply Federal reserve notes to its members?

Answer: If Bank applies for them they will be ready for delivery.

4. Can Federal reserve notes be put out by Federal reserve banks to protect their gold?

Answer: Yes. When once the Federal reserve bank has deposited the collateral and taken out the notes, it may pay out the notes for any purpose, just as any other money.

5. (a) When Federal reserve notes are called for by the Federal reserve bank, are the securities to be turned over to the Federal reserve agent?

Answer: Assuming by securities that collateral is meant, yes.

(b) Must the gold reserve behind the Federal reserve notes be turned over to the Federal reserve agent?

Answer: No. This gold reserve is precisely like any reserve against deposits, so far as its control is concerned.

(c) Must the collateral and the gold reserve be segregated and put under the joint control of the Federal reserve agent and the Governor of the bank?

Answer: As above stated, the collateral is under the control of the Federal reserve agent. The gold reserve is entirely under the control of the bank.

6. Will the Federal reserve agent have in his immediate charge unissued Federal reserve notes, or will the entire supply be carried in the Subtreasury and turned over to each bank only as called for upon order of the Comptroller?

Answer: A plan is now being prepared under which a supply of Federal reserve notes will be kept by the Federal reserve agent, as far as possible, acting as a representative of the Federal Reserve Board.

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7. Assuming that Federal reserve notes are to be issued at the opening, what will the reserve bank of Boston do if it receives on deposit a Federal reserve note, for example, of the Dallas Federal reserve bank?
Answer: It shall send this note at once to the Dallas bank for credit or redemption. Such a note could not be paid out by the Boston bank except upon a penalty of 10%.

8. Will the Federal reserve notes when delivered to the Federal reserve agent be ready for issuance or do they require the counter signature of an officer of the issuing bank?
Answer: These notes are Government obligations and when delivered will require no counter signature.

DISCOUNTS.

1. Has the Federal Reserve Board decided upon a policy which it will recommend to each reserve bank in determining the discount rate at the date of opening and thereafter?
Answer: See circular and regulations concerning commercial paper shortly to be issued.

2. Will there be several rates of discount, covering classification of paper and length of maturity?
Answer: There may be a different rate for different classes of paper and possibly for different lengths of maturity.

3. Has the Federal Reserve Board any policy to suggest in regard to paper eligible for rediscount other than that laid down in a general way in the report of the Committee on Rediscounts, adopted at the convention in Washington, October 21, 1914, which give the widest discretion to individual reserve banks?
Answer: See circular and regulations on commercial paper about to be issued.

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4. Asks whether provisions of Section 4 as to administering the bank without discrimination means anything more than the duty now imposed on the directors of any bank to deal fairly and impartially with all its customers, etc.

Answer: The above statement is a correct statement of the law.

5. Does the provision in Section 14, paragraph d, providing that rates of discount established by the Federal reserve banks shall be subject to review and determination by the Reserve Board make it necessary that the Reserve Board shall approve all rates before they are given out to the public?

Answer: Yes.

6. Section 3 provides that each Federal reserve bank shall establish branch banks. Does this make it obligatory upon the Federal reserve bank of Boston to establish branches, and, if so, when.

Answer: It will be the duty of the directors of the Federal reserve banks carefully to investigate as to the necessity for branches in its district. The Board has reasonable discretion as to such necessity and only when satisfied as to the necessity is there any obligation imposed upon the Board to establish such branches.

It is thought the question of establishing branches need not be considered at this time.

November 13, 1914.

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DRAFT OF REGULATIONS OF THE FEDERAL RESERVE BOARD, prescribing conditions under which State Banks and Trust Companies may subscribe to the stock and become members of Federal Reserve Banks.

Washington D. C._____1914.

REGULATION NO._____

Section 9 of the Federal Reserve Act reads in part, as follows:

"Any bank incorporated by special law of any State, or organized under the general laws of any State of the United States, may make application to the reserve bank organization committee, pending organization, and thereafter to the Federal Reserve Board for the right to subscribe to the stock of the Federal Reserve bank organized or to be organized within the Federal Reserve district where the applicant is located. The organization committee or the Federal Reserve Board, under such rules and regulations as it may prescribe, subject to the provisions of this section, may permit the applying bank to become a stockholder in the Federal Reserve bank of the district in which the applying bank is located. Whenever the organization committee or the Federal Reserve Board shall permit the applying bank to become a stockholder in the Federal Reserve Bank of the district, stock shall be issued and paid for under the rules and regulations in this Act provided for national banks which become stockholders in Federal Reserve banks."

Pursuant to the provisions of this section, the Federal Reserve Board prescribes the following regulations and by-laws specifying the conditions under which State banks and trust companies may become members of Federal Reserve banks.

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APPLICATION FOR STOCK.

First - Any State bank or Trust company eligible to membership in a Federal Reserve bank under the Federal Reserve Act and desiring to subscribe to the capital stock of the Federal Reserve bank organized in the district which includes the place of business of such State bank or Trust company shall under authority of its Board of Directors, to be evidenced by a proper resolution of the Board, make application for an amount of capital stock in such Federal Reserve bank equal to 6 per cent of the unimpaired capital stock and surplus of such State bank or Trust company. This application must be accompanied by a statement showing the assets and liabilities of such State bank or Trust company listed on forms approved by the Federal Reserve Board. These forms will be furnished upon request by the Chairman of the Board of the Federal Reserve bank of the district in which the applying bank is located.

The Board of Directors or a committee composed of not less than five members of the Federal Reserve Bank Board shall certify that in their opinion the assets listed in the manner prescribed by the Federal Reserve Board represent actual existing values and that in the opinion of said Board none of such assets are carried at an excessive valuation on the books of said bank.

State banks and Trust companies shall also file with their applications for membership copies of their charters, with amendments, and a digest there of showing the powers (granted by such charters and amendments) classified to indicate:

(a) Those powers which such banks and trust companies have exercised and desire to continue to exercise.

(b) Those powers which, while granted, have not been exercised and

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which such banks and trust companies will not desire nor attempt to exercise as members of the Federal Reserve System.

EXAMINATION.

Second - The Federal Reserve Board will in all cases require a special examination of the applying bank by an examiner to be designated by the Federal Reserve Board.

ASSOCIATIONS ELIGIBLE FOR MEMBERSHIP

Third - Only those banks which have an unimpaired capital sufficient to entitle them to become national banking associations under the provisions of the National Bank Act shall be considered as eligible to membership in a Federal Reserve bank.

In accordance with section 5138, U. S. Revised Statutes, as amended by the act of March 14, 1900, State banks or Trust companies in order to be eligible to membership must have unimpaired capital stock, as follows:

In cities or towns of less than 3,000 inhabitants, $25,000.

In cities or towns of more than 3,000 inhabitants but less than 6,000 inhabitants, $50,000.

In cities of more than 6,000 inhabitants but less than 50,000 inhabitants, $100,000.

In cities of more than 50,000 inhabitants, $200,000.

POWERS AND RESTRICTIONS.

Fourth - State banks becoming members as such under the provisions of Section 9 of the Federal Reserve Act and retaining their State charters shall be subject to the provisions of section 9 and to such other provisions of the Federal Reserve Act as are applicable thereto.

State banks and Trust companies may continue to exercise those banking or trust company powers, granted them by their State charters, when

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such powers are not in conflict with limitations imposed by the Federal Reserve Act. No power, however, granted by a state charter, which is not customarily exercised by a bank or trust company or which is not incident to the business of a bank or trust company, shall be exercised by any association (incorporated under the laws of any state) which becomes a member of the Federal Reserve System. The Reserve Board reserves to itself the determination as to whether these unusual powers are admissible and consistent. The applying bank must file with its application as an exhibit a statement showing powers granted to it by its State charter and those powers which it desires and intends to exercise.

INVESTMENTS BY STATE BANKS AND TRUST COMPANIES.

Fifth - Inasmuch as the Federal Reserve Act limits the amount to be loaned to any one person, firm or corporation by a State bank as a member of the Federal Reserve System but does not specifically prescribe the class and character of investments to be made, such banks or trust companies may invest in or make loans on real estate or other investments within the limitations prescribed by the laws of the State within which such bank or trust company is located, provided, such investments are so made that in due course of business they may be liquidated for an amount which will fully protect the creditors and stockholders of such associations, and no such association will be permitted to become or continue a member of the Federal Reserve System if in the judgment of the Federal Reserve Board an undue proportion of its resources are carried in such long time and

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non-liquid investments in such a proportion as to endanger the liquid conditions or the solvency of such association or to cause an impairment of its capital, and the character of all such investments will be taken into consideration in determining the value at which they may be carried on the books of the association.

CONVERTED STATE BANKS AND TRUST COMPANIES.

Sixth - Whenever a State bank or Trust company shall become converted into a national bank under the provisions of Section 8 of the Federal Reserve Act, it shall, at the same time that it files its organization certificate with the Comptroller of the Currency, execute and file with the Federal Reserve bank of its district an application for an amount of stock equal to six per cent of its unimpaired capital and surplus. If such bank or trust company desires to act as trustee, executor, administrator or registrar of stock and bonds, its application for stock in the Federal Reserve bank shall be accompanied by an application to the Federal Reserve Board for permission to exercise these powers.

Seventh - Whenever a State bank or trust company with established branches shall make application for conversion into a national bank and shall desire to retain such branches, such State bank or trust company shall comply with section 5155, U. S. Revised Statutes, which reads as follows:

"It shall be lawful for any bank or banking association organized under State laws, and having branches, the capital being joint and assigned to and used by the mother-bank and branches in definite proportions, to become a national banking association in conformity with existing laws, and to retain and keep in operation its branches, or such one or more of them as it may elect to retain; the amount of the circulation redeemable

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at the parent-bank, and each branch, to be regulated by the amount of capital assigned to and used by each."

Eighth - State banks or Trust companies applying for membership in the Federal Reserve System under section 8 of the Federal Reserve Act by conversion into national banking associations, or applying for membership under section 9 as State banks will, if otherwise found to be eligible, be given a reasonable time within which to adjust the loans and investments of such banks to conform to the requirements of the Federal Reserve Act and other laws of the United States applicable thereto. Any bank applying for membership and having loans to any one person, firm or corporation in excess of the limit allowed by the Federal Reserve Act or other loans and investments prohibited by such act shall, before being admitted to membership, give satisfactory assurance to the Committee or to the Federal Reserve Board that such loans and investments will be eliminated or made to conform to the provisions of the Federal Reserve Act and other applicable laws not later than_____.

The condition of the applying bank or trust company and the general nature of its business will be considered by the Federal Reserve Board in each case in determining whether such banks shall be admitted to membership.

Ninth - All applications must be addressed to the Federal Reserve Board but must be forwarded to the Chairman of the Board of the Federal Reserve bank of the district in which the applying bank is located, who will submit the matter to the Board of Directors of the Federal Reserve Bank of the District and in turn transmit it to the Federal Reserve Board with his recommendation and that of the Board of Directors of the Reserve Bank.

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Tenth - The Federal Reserve Board will from time to time make such amendments and adopt and publish such additional regulations and by-laws as may be deemed necessary and advisable.

FEDERAL RESERVE BOARD

BY

Governor.

Secretary.

November 13, 1914.

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EX-OFFICIO MEMBERS
WILLIAM G. McADOO
SECRETARY OF THE TREASURY
CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

W. P. G. HARDING, GOVERNOR
PAUL M. WARBURG, VICE GOVERNOR
FREDERIC A. DELANO
ADOLPH C. MILLER
CHARLES S. HAMLIN

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 14, 1914.

S I R :

Permit me to direct your attention to those records included in the accounting system adopted by the Federal Reserve Bank of which are intended for transmission to the Federal Reserve Board, and to request that you bring the matter to the attention of the proper officers, that they may see to the regular forwarding of the records intended for the Federal Reserve Board or for the Comptroller of the Currency, as the case may be. The text matter descriptive of your accounting system, which is found under the head of System 1 in Circular #7, as well as in the reproduction of this text which has been sent to the Governor of each bank, indicates clearly in the case of each form whether a duplicate is or is not to be forwarded.

It will undoubtedly require some pains at the start to see that the records are regularly transmitted at the proper time as they must be for the statistical records which the Federal Reserve Board plans to conduct in its offices as a part of its system of information, and we therefore ask you to make sure, if possible, that the matter is attended to as thoroughly as possible.

One other point in connection with the accounting system deserves mention.

In the event that member banks accounts are inactive (See form B-1) it will not be necessary to forward daily statements, and it is suggested that the ledger sheets be separated into two divisions, Active and Inactive. This would be advisable from the standpoint of economy as to postage, as well as avoiding the necessity of forwarding daily statements to a member bank whose account does not change. In the event however, of any entry being made in an inactive account, it is to be assumed that it has become active, and will be transferred to the active apportionment of accounts.

Respectfully,

Secretary.

46.

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N O T I C E .

This blank application for stock is sent to your bank direct by the Federal Reserve Board in order to save time in transmittal.

It should be returned to this office through the Federal Reserve Bank of your district.

By-laws governing conditions under which State banks and Trust companies may enter the Federal Reserve System will be forwarded as soon as available.

N O T I C E .

This blank application for stock is sent to your bank direct by the Federal Reserve Board in order to save time in transmittal.

It should be returned to this office through the Federal Reserve Bank of your district.

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#48½

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Dist.	Location of Reserve Bank	Capital (authorized)	Area in Sq. Mi.	Population	No. Member Banks	Territory Covered.
1	Boston	$ 9,711,900	66,465	6,557,841	441	Me., N.H., Vt., Mass., R. I., Conn.
2	New York	19,931,700	49,170	9,113,279	480	New York State
3	Philadelphia	12,501,500	39,865	8,110,217	758	N.J., Del., Eastern Pa.
4	Cleveland	12,101,700	183,995	7,961,022	764	Ohio, Western Pa., Northwestern West Va., Eastern Kentucky.
5	Richmond	6,387,400	173,818	8,519,313	496	D.C., Md., Va., N.C., S.C., remainder WestVa.
6	Atlanta	4,670,600	233,860	6,695,341	381	Ala., Ga., Fla., eastern Tenn., Southern Miss., Southeastern La.
7	Chicago	12,687,700	176,940	12,630,383	971	Ia., southern Wis., peninsula Mich., northern Ill., northern Ind.
8	St. Louis	4,987,500	146,474	6,726,611	459	Ark., all Mo. except extreme west, southern Ill., southern Ind., western Ky., western Tenn., northern Miss.
9	Minneapolis	4,811,000	437,930	5,724,895	709	Mont., N.D., S.D., Minn., northern Wis., remainder of Mich.
10	Kansas City	5,530,300	509,649	6,306,850	837	Kans., Nebr., Colo., Wyo., extreme West Mo., northern Okla., extreme northern N.Mex.
11	Dallas	5,698,900	404,826	5,310,561	754	Tex., remainder N.Mex., southern Okla., remainder La., southeastern Ariz.
12	San Francisco	7,775,400	693,658	5,389,303	521	Cal., Wash., Oreg., Idaho, Nev., Utah, remainder Arizona.
	TOTALS ---	$106,795,600	3,116,650	89,045,616	7,571	

November 16,1914.

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FROM THE LETTER OF A CHICAGO MANUFACTURER

on the Subject of Manufacturers Paper.

It is a well known fact that for a number of years in this country manufacturers worked on a large percentage of profit and that they did not pay as much attention to the actual cost of production as they would have had they been obliged to work on a smaller margin. The initial reason for this is that the manufacturer of today was the inventor or mechanic of yesterday, and had to work out his own solutions with limited experience and education.

The Corporation Tax Law was one of the best laws that was ever enacted, not so much from a revenue producing standpoint but from the incidental benefits due to the fact that it has made our business men and corporations, particularly the smaller ones, (which, you know, are the ones that need help and guidance) revise their methods of bookkeeping, started them to investigate their cost of production, forced them to produce a balance sheet that would show facts more clearly than they were ever shown before.

From my experience I have no hesitation in stating that a great many manufacturers are anxious to have their books record large assets, and with this end in view, they frequently capitalize such items as expenditures for jigs, tools, dies, patterns and other items.

The enormous aggregate expenditures of these items should more properly be charged as an expense of producing the article. Offering the automobile business as an illustration; the design frequently changes, in fact, often changes each year, and the jigs, tools and dies applying to, let us say the 1913 model, are of very little value for the 1914 model except insofar as they apply to repair-parts. This same condition exists in a greater or less extent in every manufacturing business. The tendency is to understate rather than over-state costs by carrying as assets tools or equipment soon rendered obsolete.

Conservative business practice would dictate that a major portion of this expense be written off as incurred and only a small percentage included in the balance sheet as representing a real asset. Of course, when a balance sheet including an asset of a large amount in respect of jigs, tools, dies, etc., is presented to a banker, it shows up very favorably and the banker accepting it at its face value, may assume a margin of safety as represented by the figures shown.

This point and others of a similar kind, all important, will come up when the new currency system is in operation. It is essential that careful consideration be given to the issuing of currency against assets

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of this nature, (i. e., commercial paper of firms or corporations doing a manufacturing business) which can hardly be regarded as realizable (liquid or quick assets) and which have little or no value in the event of a forced liquidation.

If the Federal Reserve Board insists that such corporations improve their method of recording actual operation by giving detailed information as to the character of their assets, whether of a fixed or current nature and, in the same way of their various liabilities, you will be doing the business interests of this country a great service. On this point, furthermore, Public Accountants need instruction, to the end that their certificates will give a true picture of the situation.

The great majority of business failures are due primarily to the lack of knowledge of the cost of production and selling. It is not as a general rule a question of dishonesty but of ignorance, and it is really deplorable how little some men know of what they are doing. Something should be done to assist them in attaining greater business efficiency. One way that German manufacturers have attained their high state of efficiency is through the Governmental help. The Government has not been simply a critic, but, having made a careful study of the problem, bases its regulations on a remedial and constructive policy.

The Federal Reserve Board can render invaluable service in the character of regulations promulgated in respect to manufacturers'paper and the specifications it prepares in respect to examinations by certified public accountants, classifications of assets and liabilities.

Without such rulings, examinations by public accountants will mean very little and it should be borne in mind that losses incurred on manufacturers' paper, where unsound methods are used, tend to lift the rates of interest which are paid by other manufacturers, whose methods are above reproach.

November 20, 1914.

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Federal Reserve Bank of St. Louis

November 21, 1914.

The Federal Reserve Board today made public the first consolidated statement of the Federal Reserve System. The statement as given out relates to condition at the close of business on Friday, November 20th.

Rediscounting privileges have been availed of to a considerable extent in New York, Chicago, St. Louis and Kansas City. Elsewhere the showing is much smaller. Federal Reserve notes to meet local demand have been issued principally in Chicago, New York and Minneapolis, but every bank has been supplied with an adequate quantity of notes to meet its needs. The relatively small amount of rediscounts as compared with the resources of the system is due to the policy of the Federal Reserve Board in encouraging the payment of reserve deposits in actual money instead of in rediscounted paper. Rates of rediscount established a week ago were fixed with this policy in mind as outlined in Circular #10, sometime ago issued by the Board. Reports from all districts are of the most encouraging nature and the outlook for business is stated as satisfactory. The establishment of the System has already had an important effect in increasing the lending power of the member banks in addition to the loan power of the Federal Reserve Banks.

The following consolidated statement shows in one total as nearly as available figures will permit the condition of the twelve Federal reserve banks at the close of business on November 20, 1914.

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Federal Reserve Bank of St. Louis

STATEMENT OF CASH ON HAND, REDISCOUNTS, RESERVE DEPOSITS

AND CAPITAL PAID IN

OF THE TWELVE FEDERAL RESERVE BANKS

AT THE CLOSE OF BUSINESS NOVEMBER 20, 1914.

CASH ON HAND:	
Gold coin and certificates	$203,415,000.
Legal Tender, Silver certificates and subsidiary coin.....	37,308,000.
Total.....	$240,723,000.
REDISCOUNTS:.....	$ 5,607,000.
ALL OTHER ASSETS:.....	$ 95,000.
Total.....	$246,425,000.
CAPITAL PAID IN:.....	$ 18,072,000.
RESERVE DEPOSITS:.....	227,138,000.
FEDERAL RESERVE NOTES IN CIRCULATION:.....	1,215,000.
Total.....	$246,425,000.

Gold Reserve against all liabilities	89%
Cash " " " "	105%
Cash reserve against all liabilities after setting aside 40% gold reserve against Federal Reserve Notes in circulation	105%

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Federal Reserve Bank of St. Louis

November 24, 1914.

Messrs. Warburg and Harding of the Federal Reserve Board said today:

"The story printed in a morning paper to the effect that there was a rift in the Federal Reserve Board, is absurd upon its face and without the slightest foundation.

"As the story purports to have come from members of the Federal Reserve Board in New York on Friday last, and as we are the only two members who were there at that time, having been in that city on that date to attend a meeting of the Cotton Fund Committee, we feel it our duty to make this positive and unequivocal denial."

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Federal Reserve Bank of St. Louis

Washington, D. C.

November 24, 1914.

To the Federal Reserve Board,

Gentlemen:

Your Committee which has had before it the consideration of salaries of officers of the Federal Reserve Banks begs to make the following report:

The salaries proposed by Boston are as follows:

Alfred L. Aiken, Governor	$15,000.
Frederick H. Curtiss, Federal Reserve Agent	10,000.

Your Committee recommends their approval.

The salaries proposed by New York are as follows:

Benjamin Strong, Jr., Governor	$30,000.
Pierre Jay, Federal Reserve Agent	16,000.

Your Committee recommends their approval.

The salaries proposed by Philadelphia are as follows:

Charles J. Rhoades, Governor	$20,000.
Richard L. Austin, Federal Reserve Agent	10,000.

Your Committee recommends their approval.

The salaries proposed by Cleveland are as follows:

E. R. Fancher, Governor	$16,000.
D. C. Wills, Federal Reserve Agent	10,000.

Your Committee recommends their approval.

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The salaries proposed by Richmond are as follows:

George J. Seay, Governor (includes salary as member of Advisory Council)	$15,000.
Wm. Ingle, Federal Reserve Agent	10,000.
James A. Moncure, Deputy Federal Reserve Agent	3,000.
Cashier	2,000.
Auditor	2,500.

Your Committee is unwilling to recommend these salaries. We think the salary of the Governor should not exceed, to start with, $12,000. per year.

We do not approve the salary proposed for Mr. J. A. Moncure, Deputy Reserve Agent. Mr. Moncure is a business man who does not give a great deal of his time to the bank and we think he should be paid a fair per diem - say $25 - for the actual time that he serves as Acting Federal Reserve Agent.

The salaries proposed by Atlanta are as follows:

Joseph A. McCord, Governor	$15,000.
M. B. Wellborn, Federal Reserve Agent	6,000.

Your Committee is of the opinion that the salary proposed for the Governor of the Board is excessive and should not exceed $10,000 a year. We approve the salary of the Deputy Federal Reserve Agent.

The salaries proposed by Chicago are as follows:

James B. McDougal, Governor	$20,000.
Vice-Governor	10,000.
C. H. Bosworth, Federal Reserve Agent	10,000.
W. L. McLallen, Deputy Reserve Agent	6,000.
Cashier	4,000.

Your Committee recommends their approval.

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The salaries proposed by St. Louis are as follows:

Rolla Wells, Governor,	$25,000.
William McC. Martin, Federal Reserve Agent,	10,000.
William W. Hoxton, Deputy Governor and Secretary,	7,500.
C. E. French, Cashier,	10,000.

In the opinion of your Committee, the salary roll proposed is high in comparison to most of the other Districts - possibly this is justified, but it should have consideration.

The salaries proposed by Minneapolis are as follows:

Theodore Wold, Governor,	$15,000.
John H. Rich, Federal Reserve Agent,	7,500.
P. M. Kerst, Deputy Reserve Agent, (Entire salary paid as Bank Examiner).	8,000.

Your Committee recommends their approval.

The salaries proposed by Kansas City are as follows:

Charles M. Sawyer, Governor,	No recommendation
J. Z. Miller, Federal Reserve Agent,	$ 7,500.

In respect to the salary of the Governor, no recommendation has been made.

The salaries proposed by Dallas are as follows:

Oscar Wells, Governor,	$12,000.
R. L. Van Zandt, Deputy Governor,	6,000.
E. O. Tenison, Federal Reserve Agent,	6,000.
W. F. McCaleb, Deputy Federal Reserve Agent,	4,000.
J. W. Hoopes, Cashier and Secretary,	5,000.

Your Committee recommends their approval.

The salaries proposed by San Francisco are as follows:

Archibald Kains, Governor,	No recommendation
John Perrin, Federal Reserve Agent,	$12,000.

While a salary has not been fixed for the Governor, we understand $15,000. is talked of. This we are ready to approve and Mr. Perrin's salary, originally fixed at $10,000, has been changed to $12,000.

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In regard to the compensation paid directors, your Committee recommends the following:

That the directors be allowed a fee of $20 for attending a directors' meeting, or $10 for attending meetings of the executive committee. In addition to this, directors living more than fifty miles from the Reserve banks shall be allowed a per diem fee of $10 for every day's absence from home necessarily involved in such attendance, plus necessary traveling expenses.

(Signed) F. A. Delano.

(Signed) P. M. Warburg.

(Signed) W. P. G. Harding.

Committee.

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Federal Reserve Bank of St. Louis

DEPARTMENT OF JUSTICE.

Office of the Solicitor of the Treasury,

WASHINGTON, D. C. November 24, 1914.

The Federal Reserve Board.

Gentlemen:

Referring to the so-called "Clayton Law" approved October 15, 1914, regarding monopolies, etc., I am requested to advise you whether the words "from and after two years from the date of the approval of" the said act, apply to paragraph 2 of section 8.

In other words, Mr. Robert W. Webb, Vice President of the Minneapolis Trust Company, inquires of your board by letter dated the 20th instant, whether a director of the company is eligible to serve as a director of a national bank not having common ownership of stock, until the expiration of two years after the approval of the act. And if so, may he not further serve for such time thereafter as would constitute the unexpired part of one year from the date of his election?

The first paragraph provides:

> "That from and after two years from the date of the approval of this act no person shall at the same time be a director or other officer or employee of more than one bank, banking association, or trust company, organized or operating under the laws of the United States, either of which has deposits, capital, surplus, and undivided profits aggregating more than $5,000,000, and no private banker or person who is a director in any bank or trust company, organized and operating under the laws of a State, having deposits, capital, surplus, and undivided profits aggregating more than $5,000,000, shall be eligible to be a director in any bank or banking association organized or operating under the laws of the United States."

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This paragraph further provides that -

> x x x "when a director, officer, or employee has been elected or selected in accordance with the provisions of this act it shall be lawful for him to continue as such for one year thereafter under said election or employment."

Paragraph 2 of said section provides that -

> "No bank, banking association, or trust company, organized or operating under the laws of the United States, in any city or incorporated town or village of more than 200,000 inhabitants, as shown by the last preceding decennial census of the United States, shall have as director or other officer or employee any private banker or any director or other officer or employee of any other bank, banking association, or trust company located in the same place: Provided, That nothing in this section shall apply to mutual savings banks not having a capital represented by shares: Provided further, That a director or other officer, or employee of such bank, banking association, or trust company may be a director or other officer or employee of not more than one other bank or trust company organizedunder the laws of the United States, or any state where the entire capital stock of one is owned by stockholders in the other: and provided further, That nothing contained in this section shall forbid a director of class A of a Federal reserve bank, as defined in the Federal reserve act from being an officer or director or both an officer and director in one member bank."

The last paragraph of section 8 directs that -

> "When any person elected or chosen as a director or officer or selected as an employee of any bank or other corporation subject to the provisions of this act is eligible at the time of his election or selection to act for such bank or other corporation in such capacity, his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any other provisions hereof by reason of any change in the affairs of such bank or other corporation from whatever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date of his election or employment."

From the facts stated and in accordance with my interpretation of the statute, I am of the opinion that the two years' limitation mentioned

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in the first paragraph of section 8 of the act applies also to the second paragraph, and that a director of the said trust company is eligible to serve as a director of a national bank not having common ownership of stock, until the expiration of two years after the approval of the act; and that by authority of the last paragraph above quoted, he is eligible to further serve for such time thereafter as constitutes the unexpired part of one year from the date of election.

I am of the opinion also that the statute will fairly bear the liberal interpretation that it was intended that paragraphs 1 and 2 should be read together in order that the existing arrangements might not be subject to sudden and inconvenient changes; and that the first paragraph as to eligibility to serve as a director in two institutions whose deposits, capital, etc., exceed $5,000,000, be modified by the second in the case of institutions the stock of one of which is wholly owned by the stockholders in the other.

I am further of the opinion that it was the intention of Congress that the first two paragraphs of section 8 as to banks whose deposits, capital, surplus, etc., aggregate more than $5,000,000, and as to all banks in cities of over 200,000 population, the provisions as to time of the act taking effect, mutual savings banks, common stock ownership and Federal reserve banks, should apply alike.

The letter of Mr. Webb is herewith returned.

Very respectfully,

(Signed) F. A. Reeve,

Acting Solicitor.

(Enc).

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Federal Reserve Bank of St. Louis

November 30, 1914. 67

My dear Governor:-

I am in receipt of your note of the twenty-third instant in which you submit the following questions for consideration:

Does sub-section (b), Section 14, permit a Federal reserve bank to buy United States Government bonds regardless of the limitations of Section 18?

If a reserve bank did so, could it issue Federal reserve bank notes against these bonds?

Sub-section (b) of Section 14, in defining one of the powers of the Federal reserve banks, provides in part as follows -

> "To buy and sell, at home or abroad, bonds and notes of the United States **** such purchases to be made in accordance with rules and regulations prescribed by the Federal Reserve Board".

This section taken alone vests in every Federal reserve bank the power to purchase and sell United States bonds without any limitation except such as may be imposed by regulations of the Federal Reserve Board.

Unlike Section 18, which becomes effective two years from the date of the passage of the Act, this section takes effect immediately upon the establishment of the Federal reserve banks, being a power vested in such banks when organized and authorized to commence business. It will, therefore, conduce to clearness to consider the exercise of this power, first, without reference to the provisions of Section 18 and as an independent power, and later, to consider whether the provisions of Section 18 in any way affect or restrict the provisions of this section.

It will be observed that Federal reserve banks are given the power to purchase and sell United States bonds. This power will include the purchase and sale (a) of bonds not having the circulation privilege - for example, Panama Three Per Cent bonds; (b) bonds having the circulation privilege but against which no circula-

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tion is outstanding. Such bonds to be purchased and sold as the title to this section indicates, in the open market, that is, from any source.

Section 4, sub-section 8, which likewise takes effect when the Federal reserve banks have been authorized to commence business, provides in part as follows -

> "Upon deposit with the Treasurer of the United States of any bonds of the United States in the manner provided by existing law relating to national banks, to receive from the Comptroller of the Currency circulating notes in blank, registered and countersigned as provided by law, equal in amount to the par value of the bonds so deposited, such notes to be issued under the same conditions and provisions of law as relate to the issue of circulating notes of national banks secured by bonds of the United States bearing the circulating privilege, except that the issue of such notes shall not be limited to the capital stock of such Federal reserve bank".

Under those two sections any Federal reserve bank, independently of the provisions of Section 18, may purchase in the open market United States bonds not having the circulating privilege or United States bonds having the circulating privilege but against which no circulation is outstanding and upon deposit of latter bonds in the manner provided by existing law relating to national banks, may receive from the Comptroller circulating notes in blank equal in amount to the par value of the amount so deposited.

Section 18, on the other hand, which, as stated, does not become effective until after two years from the passage of the Act, deals with a specific class of bonds, namely, those held by national banks which desire to retire in whole or in part circulating notes outstanding. This section provides in part as follows:

> "After two years from the passage of this Act, and at any time during a period of twenty years thereafter, any member bank desiring to retire the whole or any part of its circulating notes, may file with the Treasurer of the United States an application to sell for its account at par and accrued interest, United States bonds securing circulation to be retired.
>
> The Treasurer shall, at the end of each quarterly period, furnish the Federal Reserve Board with a list of such applications, and the Federal Reserve Board may, in its discretion, require the Federal reserve banks to purchase such bonds from the banks whose applications have been filed with the Treasurer at least ten days before the end of any quarterly period at which the Federal Reserve Board may direct the purchase to be made; PROVIDED, That Federal reserve banks shall not be permitted to

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"purchase an amount to exceed $25,000,000 of such bonds in any one year, and which amount shall include bonds acquired under section four of this Act by the Federal reserve bank".

The question, therefore, arises whether the limitation of $25,000,000 contained in the foregoing proviso limits the amount of United States bonds which may be purchased from any source, (e.g., bonds having no circulating privilege and bonds having circulating privilege but against which no circulation is outstanding), by a Federal reserve bank, or whether it applies only to those bonds which are offered for sale by a member bank through the Treasurer of the United States with the intent to contract the circulation of such member bank. The language of this proviso is somewhat ambiguous since the enacting clause provides that -

"The Federal Reserve Board may, in its discretion, require the Federal reserve banks to purchase such bonds (that is, bonds which are offered for sale through the Treasurer by member banks)",

while the language of the proviso is

"Provided that the Federal reserve banks shall not be permitted to purchase an amount to exceed $25,000,000 of such bonds (that is, bonds offered for sale by member banks as above indicated) in any one year, and which amount shall include bonds acquired under Section 4 of this Act by the Federal reserve bank".

"Provided, further, that the Federal Reserve Board shall allot to each Federal reserve bank such proportion of such bonds as the capital and surplus of such bank shall bear to the aggregate capital and surplus of all the Federal reserve banks".

If we analyze this language we find (1) that the power is vested in the Federal Reserve Board to require Federal reserve banks to purchase bonds offered for sale, after two years from the passage of the Act, by member banks through the Treasurer of the United States. (2) By way of limitation to the exercise of this power by the Federal Reserve Board, Federal reserve banks are not permitted to purchase more than $25,000,000 of such bonds in any one year. That is to say, the combined or aggregate purchases of all Federal reserve banks of bonds offered for sale through the Treasurer of the United States, and which the Federal Reserve Board may require the several Federal reserve banks to purchase in proportion to the capital and surplus of such banks, shall not exceed $25,000,000 in any one year, and to quote from the statutes -

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"this amount shall include bonds acquired under Section four of this Act by the Federal reserve bank."

It will be observed -

First - that the amount to be included in the $25,000,000 referred to is the amount of bonds acquired under Section four which defines the general corporate powers of a Federal reserve bank, and includes in such powers the right on the part of the Federal reserve bank to deposit with the Treasurer of the United States bonds bearing the circulating privilege and to receive therefor circulating notes.

No reference is made in this proviso to Section 14 which authorizes banks to purchase in the open market United States bonds either with or without this circulating privilege. Section 18 deals with bonds which not only have the circulating privilege but against which circulation is already outstanding. This is significant because the question of contraction is unquestionably involved and the limitation imposed seems to be a limitation on the amount of bonds which the Federal reserve banks may be required to purchase from member banks in order to permit such member banks to reduce the amount of their outstanding circulation.

In other words, Section 18 may be said to be supplementary to the Act approved July 12, 1882 as amended by the Act approved March 4, 1907, providing for the withdrawal of circulating notes on deposit of lawful money, and the withdrawal of bonds, which Act reads in part as follows -

> "Provided that not more than nine million dollars of lawful money shall be so deposited during any calendar month for this purpose".

In other words, Section 18 provides an additional method by which member banks may reduce their outstanding circulation to the extent of $25,000,000 a year by the sale of such bonds to Federal reserve banks to this amount, provided, such Federal reserve banks have not lost their power to purchase such bonds from member banks by purchases made in the open market.

Second - It will also be observed that the amount to be included in the $25,000,000 referred to is the amount of bonds required under Section four by one Federal reserve bank and not by the several Federal reserve banks which language, as above stated, is ambiguous. It may be that this is the result of a typographical error and that Congress intended that section to read -

> "This amount shall include bonds acquired under Section four of this Act by the Federal reserve banks",

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in which case it would still seem clear that Section 18 is independent of Section 14 and that the limitation imposed by Section 18 applies only to the amount of bonds which the several Federal reserve banks may be required to purchase in order to enable member banks to reduce their outstanding circulation to the extent of $25,000,000 a year in addition to the amount now allowed by law, namely, nine million dollars per month.

On the other hand, if we assume that Congress intended to confine the amount to be included to the amount of bonds purchased by one Federal reserve bank, this ambiguity is partly explained by a consideration of the language of this particular section as it passed the Senate and as it finally appeared in the Act when passed by Congress. In the bill as it passed the Senate on December 19th, 1913, this section provided that -

> "The Federal Reserve Board may, in its discretion, require the Federal reserve banks to purchase <u>such</u> bonds from the banks whose applications have been filed with the Treasurer at least ten days before the end of any quarterly period at which the Federal Reserve Board may direct the purchases to be made".

No limitation was placed upon the amount of such bonds which the Federal Reserve Board might, in its discretion, require the several Federal reserve banks to purchase.

As amended by the Conference Committee of the Senate and House, the amount of such bonds which the several Federal reserve banks are permitted to purchase is limited to $25,000,000 in the aggregate in any one year, such bonds being those held by member banks and having circulation outstanding against them.

Without the language which follows this limitation and which reads "<u>And which amount shall include bonds acquired under Section four of this Act by the Federal reserve bank</u>", the word "<u>permitted</u>" would be synonomous with the word "<u>required</u>," that is to say, the same result would obtain if the proviso read "<u>the Federal reserve banks shall not be required to purchase an amount to exceed $25,000,000 of such bonds in any one year</u>".

Since in this case the limitation would have applied to the power of the Federal Reserve Board to require the purchase of such bonds, while the Act as it passed effects the same result by limiting the power of the bank to purchase instead of limiting the power of the Board to require such bank to exercise the power to purchase.

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The question, therefore, arises - what is the effect of the language "and which amount shall include bonds acquired under Section 4 of this Act by the Federal reserve bank."

As above stated, it will be observed that the purchases to be included in the $25,000,000 are the purchases of one bank, not the aggregate purchases of the several Federal reserve banks, and this language would be difficult to explain without the aid of the second proviso which follows and which reads:

> "Provided, further, that the Federal Reserve Board shall allot to each Federal reserve bank such proportion of such bonds as the capital and surplus of such bank shall bear to the aggregate capital and surplus of all the Federal reserve banks".

Considering this language as part of the context the conclusion seems inevitable that Congress intended that no part of the $25,000,000 in bonds which the Federal Reserve Board might require the several Federal reserve banks to purchase through the Treasurer from member banks shall be allotted to a Federal reserve bank which had purchased under Section 4 United States bonds equal to or in excess of the amount which would otherwise be allotted to such bank, and had taken out Federal Reserve bank notes against said bonds.

Unless this view is adopted, it would be difficult to attach any meaning to the proviso that the $25,000,000 should include bonds acquired under Section 4 of this Act "by the Federal reserve bank".

The meaning of these provisions would perhaps be clearer if they should be transposed to read -

> "Provided, the Federal Reserve Board shall allot to each Federal reserve bank such proportion of such bonds as the capital of such bank shall bear to the aggregate capital and surplus of all the Federal reserveve banks".
>
> "Provided, further, that Federal reserve banks shall not be permitted to purchase an amount to exceed $25,000,000 of such bonds in any one year, and which amount shall (in making such allotments) include bonds acquired under Section 4 of this Act by the Federal reserve bank (to which such allotment is made)."

It is significant that throughout both provisions the language "such bonds" is consistently used. The bonds referred to as "such bonds", of which Federal reserve banks are permitted to purchase an amount not to exceed $25,000,000

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in any one year, are shown by the context to be bonds offered by member banks for sale through the Treasurer in order to reduce the circulation of such member banks, and also which form a part of an aggregate amount which the Federal Reserve Board may require the Federal reserve banks to purchase.

These elements are necessary to bring such bonds within the purview of this section. The limitation prescribed is the limitation of the amount which the Federal Reserve Board may require Federal reserve banks to purchase, and it seems clear that if a Federal reserve bank has under the power contained in Section 14 already purchased United States bonds with the circulation privilege equal to or in excess of what its allotment would otherwise be, and has taken out Federal reserve bank notes against such bonds, under Section 4, it is not permitted or required to share in the purchase of such bonds which must be purchased at par.

If we assume that Congress intended to include bonds purchased by the several Federal reserve banks under Section 4 in the limitations prescribed, the effect would be that if any number of the Federal reserve banks had purchased in the open market in the aggregate bonds having the circulating privilege of $25,000,000 in any one year, then no Federal reserve bank would be permitted to purchase any bonds offered by member banks for sale through the Treasurer of the United States.

If, on the other hand, we follow the language of the Act and interpret it as aforesaid, the effect would be that if some of the Federal reserve banks had purchased in the open market no bonds having the circulation privilege during the year they might be required to take their allotment of this $25,000,000, while those banks which had purchased bonds equal to or in excess of the amount to which they would be entitled, would not be permitted to purchase any such bonds, if those purchased in the open market had been used as a basis of an issue of Federal reserve bank notes.

In either view, the conclusions seem fully justified -

First - That Federal reserve banks may, under Section 14, sub-section (b), purchase in open market United States bonds with or without the circulating privilege, to such an extent as the Federal Reserve Board may by regulation permit, and without reference to the limitations of Section 18.

Second -That any bonds so acquired, having the circulating privilege, may, under the provisions of Section 4, be deposited with the Treasurer of the United States as a basis for issue of Federal reserve bank notes.

Third - That after two years from the passage of the Act any bonds against which national banks have outstanding national bank notes, may be purchased by Federal reserve banks when offered for sale through the Treasurer of the United States,

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provided, that the Federal reserve bank to which an allotment is made has not already purchased in the open market bonds with circulation privilege equal to or in excess of the amount to which it would be entitled, and has taken out Federal reserve bank notes against such bonds under Section 4, or, if it is assumed that the limitation of bonds purchased by one Federal reserve bank was the result of a typographical error, then, provided the several Federal reserve banks have not already purchsed in the aggregate in open market such bonds amounting to $25,000,000, and have used bonds so purchased as security for an issue of Federal reserve bank notes. Inasmuch, however, as the language can be given a meaning without this assumption, there would seem to be no justification for treating this as a typographical error.

Fourth - That until a period of two years from the passage of this Act has expired, Federal reserve banks purchasing in open market bonds having the circulating privilege may deposit same with the Treasurer of the United States and obtain an issue of Federal reserve bank notes on the security of such bonds.

Fifth - That after two years from date of the passage of the Act Federal reserve banks acquiring bonds bearing the circulating privilege under Section 14 or Section 18 may, under the provisions of Section 18 which becomes effective at that time, procure an issue of Federal reserve bank notes on the security of such bonds, or, may, with the approval of the Federal Reserve Board, exchange any such United States two per cent gold bonds bearing the circulating privilege (if such bonds have no circulation outstanding) for one year gold notes of the United States without the circulating privilege to an amount not to exceed one-half of the bonds so tendered for exchange, and thirty year three per cent gold bonds without the circulating privilege for the remainder of the two per cent bonds so tendered, subject to the limitations prescribed in Section 18.

Respectfully,

Counsel.

Hon. Charles S. Hamlin,
GOVERNOR.

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#67

Washington, D. C.,
December 3rd, 1914.

The Examination and Audit of Federal Reserve and Member Banks under the direction of the Federal Reserve Board.

There has been created a Division of Audit and Examination. As an outline of its duties the following is submitted for the information of all concerned:

1. EXAMINATION AND AUDIT OF FEDERAL RESERVE BANKS.

(a) Federal reserve banks.

(b) Books and accounts of Federal reserve agents.

(a) Federal Reserve Banks.

Sec. 11; Par A - Authorizes and empowers the Federal Reserve Board "To examine at its discretion the accounts, books and affairs of each Federal Reserve Bank."

Sec. 21; Par. 5 - Provides that the "Federal Reserve Board shall, at least once each year, order an examination of each Federal reserve bank, and upon joint application of ten member banks the Federal Reserve Board shall order a special examination and report of the condition of any Federal reserve bank."

The law provides for an examination of each Federal reserve bank at least once a year, but it is proposed that examinations shall be held ordinarily twice each year, covering a thorough investigation of rediscounts, collateral loans, investments and open-market transactions, particular attention being paid to compliance with the provisions of the Federal Reserve Act and regulations promulgated by the Federal Reserve Board.

Paper accepted for rediscount should be analyzed, in order to determine its eligibility under the regulations

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issued. Inquiry should also be made as to the condition of member banks offering paper for rediscount. Every examination should cover a complete audit of the bank and a report made to the Federal Reserve Board as to the condition of each bank, competency of management, adequacy of records and attention given by the directors to the affairs of the reserve bank. Attention should be called to any unsafe or unsound condition, or any vicious tendency that might appear in any department of the bank.

(b) Federal Reserve Agent.

> Section. 11; Par I - The Federal Reserve Board shall be authorized "to require bonds of Federal reserve agents, to make regulations for the safeguarding of all collateral, bonds, Federal reserve notes, money or property of any kind deposited in the hands of such agents, * * * and make all rules and regulations necessary to enable said board effectively to perform the same."

The records and accounts of the Federal reserve agent in each Federal reserve district shall be examined at least quarterly, and a complete report made to the Federal Reserve Board. The examination shall cover a verification of the money, Federal reserve notes and collateral in the hands of the Federal reserve agent.

2. SPECIAL EXAMINATIONS OF MEMBER BANKS OR BANKS APPLYING FOR MEMBERSHIP.

(A) Member Banks.

> Sec. 11; Par. A - The Federal Reserve Board shall be authorized "to examine at its discretion the accounts, books and affairs of each Federal reserve bank and of each member bank."

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It is expected that the exercise of this function will be confined to special examinations or investigations to be made only when deemed necessary by the Federal Reserve Board, or with the approval of the Board upon a request by any Federal reserve bank. The primary purpose of such examination should be to ascertain the condition of a member bank or of the lines of credit which are being extended by it.

The Federal Reserve Act also grants authority to the Comptroller of the Currency and to the Federal reserve banks the right to examine member banks. Therefore, in order to prevent confusion and secure co-operation and coordination with the examinations of National banks by the examiners on the staff of the Comptroller of the Currency and in order to avoid duplication in examinations a plan has been suggested, details of which are embodied in the report of a special committee on this subject appointed by the Comptroller acting with a committee of your Board to suggest a means of standardizing the salaries of National bank examiners and the method of assessing banks for the cost of such examinations. A copy of that portion of the report relating to the matter above referred to is attached to this memorandum.

(B) State Institutions Applying for Membership.

> Sec. 9; Par. 2.- "The Organization Committee or the Federal Reserve Board shall establish by-laws for the general government of its conduct in acting upon applications made by the State banks and banking associations and trust companies for stock ownership

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> in Federal reserve banks. Such by-laws shall require applying banks * * * to submit to the examination and regulations prescribed by the Organization Committee or by the Federal Reserve Board." *

The examinations of such institutions shall be made when ordered by the Federal Reserve Board. It is recommended, however, that all such applications shall be referred to the Division of Audit and Examination, which shall communicate with the Reserve bank of the District and with the State banking authorities. In connection with this inquiry, the Division of Audit and Examination shall be authorized to call for such supplemental information as may be deemed necessary, for example, the following:

(1) A copy of report of the last examination by State authorities;
(2) Loans over a stated amount;
(3) Real estate investments, loans secured by real estate collateral, loans secured by stock of real estate corporations, real estate mortgages with data as to maturities;
(4) The business, firm and corporation affiliations of officers and directors;
(5) A de ailed statement of investments.

(C) Special Examinations - State Banks and Trust Company Members.

> Sec. 21; Par. 1.- The Federal Reserve Board "may authorize examination by the State authorities to be accepted in the case of State banks and trust companies and may at any time direct the holding of a special examination of State banks or trust companies that are stockholders in any Federal Reserve Bank."

The intent of the law seems to be to accept the examination made by State authorities wherever it can be

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done without discrimination. It should therefore be a function of this Division to investigate the examining methods of State authorities, in order to ascertain whether or not the standard of examinations is such as to be acceptable to the Federal Reserve Board.

It will be necessary to request State authorities to furnish the Federal reserve banks information as to the condition of each State institution that is a member of the Federal Reserve System. Whenever a special examination is necessary by either the Federal Reserve Board or a Federal reserve bank it is usually desirable that such examination should be made in connection with an examination made by State authorities.

3. SPECIAL INVESTIGATIONS.

Special investigations will be held only when deemed advisable or order by the Reserve Board, either when warranted by general business or other conditions. Applications for the establishment of domestic or foreign branches, or of member banks to exercise trust company powers shall be investigated by this Division.

4. CREDIT BUREAUS.

The establishment of credit bureaus in Federal reserve banks, and of a central credit bureau at Washington is so closely related to examinations, that it is desirable that the Division of Audit and Examination

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shall be responsible for the development of the system. The purpose of the credit bureau is to collect and record data concerning member banks and the standing of individuals, firms and corporations discounting at and borrowing from these banks, or selling paper to them. Furthermore, it is very desirable that credit bureaus be established in each Federal reserve bank, under the joint supervision of the Federal Reserve Agent and the Governor of the Bank, in order that material may be there collected, recorded and indexed for the benefit of the board of directors or Executive Committee passing upon the paper offered for rediscount, and open for inspection by examiners of the Federal Reserve Board.

Under the accounting system which has been adopted reports of various loans made are reported daily to the Washington office. It is proposed a few months hence to require a further weekly report giving the aggregate liability of the makers or payers of the paper rediscounted. This data will then be analyzed at the Washington office and recommendations made which will assist the credit bureaus of the different districts. It will be necessary to establish a system of co-operation and interchange of information between the district credit bureaus and also establish co-operation between National bank examiners and the Federal reserve banks in each district. This subject is more fully covered in the

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report of the committee of examiners to the Comptroller and the Federal Reserve Board, to which reference is now made.

5. REPORTS AND STATEMENTS.

Various detailed and periodical reports are forwarded to the Federal Reserve Board by the reserve banks. Information as to rediscounts and loans is received daily and the figures recorded on the records of the Division of Reports and Statistics. Loan reports will require careful analysis. The work of the Division of Reports and Statistics and that of the Division of Audit and Examination are so closely related that it is esential that close cooperation shall exist between the two.

6. AUDIT.

The Board will determine later whether it will include under the Division of Audit and Examination a Department for audit of bills for its own purchase of material, or disbursements.

Staff of the Division of Audit and Examination.

The Board does not contemplate making general examinations until January, 1915. The number of men who will be required on this work will depend entirely upon the extent of the special examinations and investigations demanded, and it is expected to draw upon the staff of the Comptroller of the Currency for assistance in these examinations.

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For the routine work of examination, three to four Federal reserve examiners and say two assistant examiners will be necessary. An auditing clerk will be required to pass upon the bills for disbursement; a report clerk to analyze the reports made by the Federal reserve banks and record loan data on the Credit Bureau records will be needed. At least one stenographer will be required for the use of the Division.

Submitted to the Board
On Behalf of the Committee on
Audit and Examination.

Adopted by the Federal Reserve Board
December 18, 1914.

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EXAMINATION OF MEMBER BANKS.

1. Section 11, Par. 4. The Federal Reserve Board shall be authorized:
(a) "To examine at its discretion the accounts, books, and affairs of each Federal Reserve Bank and of each member bank."

11. Section 21, Par.1 provides that "The Comptroller of the Currency, with the approval of the Secretary of the Treasury, shall appoint examiners who shall examine every member bank at least twice in each calendar year and oftener if considered necessary. The Federal Reserve Baord may authorize examination by State authorities to be accepted in case of State Banks and Trust Companies."

111. Section 21, Par.3. provides that "In addition to the examination made and conducted by the Comptroller of the Currency, every Federal Reserve Bank may, with the approval of the Federal Reserve Agent or the Federal Reserve Board provide for special examination of member banks within its district. * * * Such examinations shall be so conducted as to inform the Federal Reserve Bank of the condition of its member banks and of the lines of credit which are being extended by them."

The law requires that two examinations of every member bank shall be made in each calendar year by examiners appointed by the Comptroller of the Currency. An exception is made, however, in State Banks and Trust Companies where the Federal Reserve Board has authorized the acceptance of examinations by State authorities. It will be seen further that the Federal Reserve Act gives to the Federal Reserve Board the power to examine each member bank, and also that each Federal Reserve Bank has the power to examine its member banks.

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At present many banks supplement Federal or State examination by independent examinations by clearing house examiners, public accountants or directors. State institutions are examined by State bank examiners and under the laws of some States compulsory examinations by directors are also required.

If advantage is taken of the right to examine member banks, by all of the authorities upon whom the power is conferred, it will place member banks under continuous examination, at a tremendous expense, cause duplication and confusion, and defeat the purpose which the law is intended to serve. The law contemplates not an increase in examinations but rather an increase in the effectiveness of examinations in both city and country districts.

SUGGESTIONS AS TO EXAMINATIONS - MEMBER BANKS.

(a) National Bank Examinations.

It is plainly the intent of the law that all regular examinations of member banks shall be made by national bank examiners. The Act permits the Federal Reserve Board to accept examinations by State authorities as to State banks and trust companies admitted to the Federal Reserve System.

The primary purposes of all examinations are to ascertain that the institutions are solvent, that business is being conducted in accordance with the law, and to correct unsafe and unsound tendencies.

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(b) Federal Reserve Bank Examinations.

The primary purpose of such examinations is to "inform the Federal Reserve bank of the condition of its member banks and of the lines of credit which are being extended by them".

In order to determine the line of rediscount which may be safely and wisely extended, the Federal reserve bank in each district will be interested in obtaining detailed information concerning each member bank, as to financial condition, character of management, competency of officers and directors, care exercised in granting and checking credits, customs in extending accomodation to directors and officers, or to corporations which they may own, control or be interested in, and relations with large borrowers.

The necessary information could be obtained by the national bank examiners in connection with the regular examination. If the plan of co-operation is approved, it is suggested that the Federal Reserve Agent be furnished with -

1. Record of loans over a stated amount as shown at each examination in order that the data may be recorded on the Credit Bureau records and made available for future reference.

2. Such other information as may be desired by the Federal Reserve bank.

3. Copies of the reports of examinations of member banks, upon request made to the Supervising National Bank Examiner of the district. These copies to be later returned to the Supervising Examiner.

Under the proposed plan of co-operation between the Federal reserve banks and the National Bank Examination system information will be obtained by the examiners for the use of each Federal reserve bank. On the other hand, the records will be available to the examiners for use at subsequent examinations. Each bank will have a record of the business, firm and corporation affiliations of directors and officers of each member bank; credit information concerning member banks and the standing of borrowers, and record of failures and bankruptcies. The loan lists, after being recorded on Credit Bureau records will be returned for use at following examinations.

If a special examination by an examiner appointed by a Federal reserve bank, is thought to be necessary, it should be made, whenever possible, in connection with the regular examination made by national or State examiners, but under no circumstances without the approval of the Federal Reserve Board.

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(c) Federal Reserve Board - examination of member banks.

The exercise of this function should be confined to special examinations or investigations, to be made when and as deemed necessary by the Federal Reserve Board, or with the approval of the Board upon a request made by any Federal reserve bank. It will frequently be desirable to have the examination made by national bank examiners acting under assignment or instructions from the Comptroller of the Currency in cooperation with the Federal Reserve Board.

EXPENSES OF EXAMINATION.

Federal Reserve Board Examinations.

Section 10 of the Federal Reserve Act provided that "The Federal Reserve Board shall have power to levy semi-annually upon the Federal reserve banks, in proportion to their capital stock and surplus, an assessment sufficient to pay its estimated expenses and the salaries of its members and employees".

It is apparent that the expenses of examinations made by direction of the Federal Reserve Board must be provided for in the semi-annuall assessment above referred to. In connection with the preliminary examination of State institutions seeking admission, it may be possible to charge the institutions investigates the actual expenses incurred.

December 3, 1914.

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To be released December 6, 1914.

November 21st, 1914.

SUBJECT: Interpretation of Section 8 of the Act approved October 15, 1914.

My dear Governor:-

A number of letters have been received from bankers and others asking for an interpretation of Section 8 of the Act approved October 15, 1914, and generally referred to as the Clayton Act. Section 8 reads as follows -

"That from and after two years from the date of the approval of this Act no person shall at the same time be a director or other officer or employee of more than one bank, banking association or trust company, organized or operating under the laws of the United States, either of which has deposits, capital, surplus, and undivided profits aggregating more than $5,000,000, and no private banker or person who is a director in any bank or trust company, organized and operating under the laws of a State, having deposits, capital, surplus, and undivided profits aggregating more than $5,000,000, shall be eligible to be a director in any bank or banking association organized or operating under the laws of the United States. The eligibility of a director, officer or employee under the foregoing provisions shall be determined by the average amount of deposits, capital, surplus, and undivided profits as shown in the official statements of such bank, banking association, or trust company filed as provided by law during the fiscal year next preceding the date set for the annual election of directors, and when a director, officer, or employee has been elected or selected in accordance with the provisions of this Act it shall be lawful for him to continue as such for one year thereafter under said election or employment.

"No bank, banking association or trust company organized or operating under the laws of the United States in any city or incorporated town or village of more than two hundred thousand inhabitants, as shown by the last preceding decennial census of the United States, shall have as a director or other officer or employee any private banker or any director or other officer or employee of any other bank, banking association or trust company located in the same place: PROVIDED, That nothing in this section shall apply to mutual savings banks not having a capital stock represented by shares: PROVIDED, FURTHER, That a director or other officer or employee of such bank, banking association, or trust company may be a director or other officer or employee of not more than one other bank

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or trust company organized under the laws of the United States or any State where the entire capital stock of one is owned by stockholders in the other; AND PROVIDED FURTHER, That nothing contained in this section shall forbid a director of Class "A" of a Federal reserve bank, as defined in the Federal Reserve Act, from being an officer or director or both an officer and director in one member bank.

"That from and after two years from the date of the approval of this Act no person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000, engaged in whole or in part in commerce, other than banks, banking associations, trust companies and common carriers subject to the Act to regulate commerce, approved February fourth, eighteen hundred and eighty-seven, if such corporations are or shall have been theretofore, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the anti-trust laws. The eligibility of a director under the foregoing provision shall be determined by the aggregate amount of the capital, surplus, and undivided profits, exclusive of dividends declared but not paid to stockholders, at the end of the fiscal year of said corporation next preceding the election of directors, and when a director has been elected in accordance with the provisions of this Act, it shall be lawful for him to continue as such for one year thereafter.

"When any person elected or chosen as a director or officer, or selected as an employee of any bank or other corporation subject to the provisions of this Act is eligible at the time of his election or selection to act for such bank or other corporation in such capacity his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the affairs of such bank or other corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date of his election or employment".

It will be observed that paragraph one and paragraph three each begins "That from and after two years from the date of the approval of this Act", while paragraph two contains no such provision. The question has accordingly been raised whether or not paragraph two becomes immediately effective or after the expiration of two years from the approval of the Act. An analysis of this section

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will show that paragraph one and paragraph two both deal with the question of qualification of directors serving on the Boards of banks organized under the laws of the United States while paragraph three has reference to corporations engaged in whole or in part in commerce and to common carriers.

Paragraph one and paragraph three each begins with the word "That" which introduces the grammatical object of the enacting phrase, and as the second paragraph has no such introductory word and deals with the same general subject matter as paragraph one, it seems entirely clear that paragraphs one and two constitute one enactment and that the provisions of paragraph two become effective at the same time as the provisions of paragraph one,- namely, two years after the passage of the Act. This view is borne out by an analysis of paragraphs one and two.

Paragraph one provides in effect that no person shall at the same time be a director, officer or employee of more than one bank organized or operating under the laws of the United States, if such person is a director, officer or employee of a bank having aggregate resources of more than five million dollars. If such person is a director, officer or employee of a state bank having aggregate resources of more than five million dollars, he shall not be eligible to serve as a director, officer or employee of any bank organized or operating under the laws of the United States.

Paragraph two provides in effect that no person shall be a director in a bank organized under the laws of the United States and located in a city of more than two hundred thousand inhabitants if such person is a director of any other bank, banking association or trust company located in the same place. There are certain exceptions to this provision, namely -

(a) Mutal savings companies having no capital stock are excluded.

(b) Class "A" directors of Federal reserve banks may serve as directors of other banking institutions in the same place.

(c) A director, officer or employee of one banking association in such city may be a director, officer or employee of not more than one other bank or trust company organized under the laws of the United States where the entire capital of one is owned by stockholders in the other.

It will, therefore, be observed that these two paragraphs relate to the question of what persons are eligible to serve on the Board of Directors of a bank organized under the

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laws of the United States, or to serve in the capacity of officer or employee of such bank.

This being a Federal statute it cannot, of course, relate to the qualifications of state bank directors but merely provides that persons who are directors of state banks under certain conditions shall be ineligible to serve as directors of banks organized under Federal law, and since both paragraphs relate to this one subject, there would seem to be no justification for treating them separately as there is nothing to indicate that they constitute two separate enactments.

Respectfully,

(Signed) M. C. Elliott.

Counsel.

Hon. Charles S. Hamlin,
Governor.

12/5/14.

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December 9, 1914.

REGULATION NO. 9.

THE DUTIES OF THE FEDERAL RESERVE AGENTS WITH RELATION TO FEDERAL RESERVE NOTES.

(1) Federal Reserve Agents shall from time to time notify the Federal Reserve Board on a standard form, Form No.( ) and as far in advance as practicable, of the supply of Federal reserve notes they expect to require in order to meet applications for issue, stating the amounts of the different denominations desired.

(2) The Federal Reserve Board will determine to what extent notes shall be supplied to Federal Reserve Agents and will notify them that they are authorized to issue notes so supplied from time to time to their respective banks in response to applications duly approved by said agents.

(3) The Federal Reserve Agent shall from time to time notify his Federal Reserve Bank of the extent to which he is authorized to meet its applications for Federal reserve notes.

(4) A Federal Reserve Bank desiring an issue of Federal reserve notes shall make application therefor to its Federal Reserve Agent furnishing at the same time to said Agent a list of the collateral which it proposes to tender as a deposit against said notes, said application to be made out on Form B.D. 21-1.

(5) The Federal Reserve Agent shall carefully examine the collateral and make such investigation as he may deem necessary. If satisfied that the collateral conforms to provisions of Section 13 of the Federal Reserve Act and the Regulations of the Federal Reserve Board made pursuant thereto, he shall so inform the Federal Reserve Bank and shall notify said bank that Federal reserve notes will be issued as soon as the collateral is deposited and the requisite gold redemption fund paid to the Treasurer of the United States, and the required gold reserves set apart by said bank. (*)

(6) On receipt of said collateral and a certificate from the Treasurer of the United States setting forth that the Federal Reserve Bank has deposited with him the requisite gold redemption fund, the Federal Reserve Agent if satisfied that the bank has the gold reserve in its vault required by law to be held against its notes, shall issue, to extent

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(*) Note: Under Section 16 of the Federal Reserve Act, this redemption fund may be increased above the 5% legal minimum at the discretion of the Secretary of the Treasury.

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that such issue has been authorized by the Federal Reserve Board, Federal reserve notes to said bank, receipting for said collateral on Form B.D. 21-2, reporting to the Federal Reserve Board each day all notes issued to and withdrawn by said bank, using for that purpose Form F.R.A.5, and notifying said Board of the collateral accepted, using for that purpose Form B.D. 21-3.

(7) If at any time the Federal Reserve Agent deems it necessary to require changes in either the character or amount of collateral deposited to protect said notes, he shall notify the Federal Reserve Board and at the same time call upon the Federal Reserve Bank for additional collateral or new collateral to be substituted for that which in his opinion or in the opinion of the Federal Reserve Board is unsatisfactory, using for that purpose the Forms already referred to.

(8) If at any time the gold reserve required by law to be held by a Federal Reserve Bank against Federal reserve notes issued to it falls below 40% (including therein the gold fund required to be maintained in the Treasury) the Federal Reserve Agent shall at once notify the Federal Reserve Board.

(9) The Federal Reserve Board will, upon receipt of notice provided in Paragraph 8 hereof, establish a graduated tax as provided in Section 11 of the Federal Reserve Act upon such deficiency, which tax shall be computed and collected by the Federal Reserve Agent and forwarded to the Federal Reserve Board. Said tax shall be computed as follows:

When reserves fall below 40% but are in excess of 32-1/2%, the tax upon the deficiency shall be at the rate of 1% per annum;

When reserves fall below 32-1/2% but are in excess of 30%, the tax on the entire deficiency below 40% shall be at the rate of 2-1/2% per annum;

When reserves fall below 30% but exceed 27-1/2% the tax upon the entire deficiency below 40% shall be at the rate of 4% per annum.

and so on, increasing at the rate of 1-1/2% with each reduction in reserve amounting to 2-1/2% or any fraction thereof.

Gold Reserves against Fed'l Reserve Notes	Penalty Tax on Deficiency in Reserves.
40%	(Legal Minimum including Redemption
37½%	1 % Fund).

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Gold Reserves against Fed'l. Reserve Notes.	Penalty Tax on Deficiency in Reserves.
35 %	1 %
32½"	1 "
30 "	2½"
27½"	4 "
25 "	5½"
22½"	7 "
20 "	8½"
17½"	10 "
15 "	11½"
12½"	13 "
10 "	14½"
7½"	16 "
5 "	17½"
2½"	19 "
0	20½"

(10) The Federal Reserve Agent shall receive Federal reserve notes unfit for circulation presented by the reserve bank or any member bank or transmitted to him by the Treasurer of the United States, and shall forward the same immediately to the Comptroller of the Currency for cancellation and destruction using Forms F.R.A.1-5. The Comptroller will transmit new notes in lieu thereof to the Federal Reserve Agent, at the same time notifying the Federal Reserve Board of such action. (See also Paragraphs 16-17-18)

(11) The Comptroller will cancel and destroy such notes unfit for circulation in the manner provided in the National Bank Act for the cancellation and destruction of National bank notes unfit for circulation.

(12) The Federal Reserve Board will maintain a record of the amounts of notes of the several denominations supplied to each Federal Reserve Agent, of the amounts issued through said agent to his Reserve Bank, and of the amounts in the possession of said agent.

(13) On the receipt of notice from the Federal Reserve Board that a rate of interest has been established to be charged upon issues of Federal reserve notes, the Federal Reserve Agent shall notify his bank and shall compute and collect the amount of interest due from said bank and forward the same to the Reserve Board.

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(14) When Federal reserve notes issued by the Federal Reserve Agent to a Federal Reserve Bank are deposited by said bank for the purpose of reducing its liability for outstanding circulation, the Federal Reserve Agent shall return to said bank a proportionate amount of the collateral deposited by it against its notes, using for this purpose Form B.D.28-1.

(15) The Federal Reserve Agent shall notify the Federal Reserve Board of any deposits made with him by a Federal Reserve Bank of its own Federal reserve notes, or of gold, gold certificates or lawful money, for the purpose of reducing its liability against its outstanding notes, using for that purpose Form F.R.A.5.

(16) The Federal Reserve Agent shall hold such notes gold, gold certificates or lawful money so deposited, subject to the order of the Federal Reserve Board. Any gold or gold certificates deposited with a Federal Reserve Agent may be deposited in the nearest sub-treasury of the United States, (with the consent of the Secretary of the Treasury) and he may receive in exchange therefor gold certificates made payable to the order of said Federal Reserve Agent.

(17) On deposit of such notes, gold, gold certificates or lawful money, a proportionate amount of the collateral may be returned to said bank, the transaction to be reported at once to the Federal Reserve Board, using for that purpose Form F.R.A.5.

(18) When Federal reserve notes are deposited by a Reserve Bank with the Federal Reserve Agent, said agent shall return to said bank the collateral and any gold, gold certificates or lawful money deposited by it to reduce liability except so much of said gold as he may have been required by the Federal Reserve Board to transmit to the Treasury for redemption purposes, upon request of the Secretary of the Treasury.

(19) On receipt of notice from a Federal Reserve Agent, that certain of its notes have been returned, the Federal Reserve Board will request the Secretary of the Treasury to direct the Treasurer of the United States to return to said bank such portion of its redemption fund as may be in excess of the minimum amount required to be maintained by said bank in the gold redemption fund against its notes still outstanding.

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(20) When a Federal Reserve Bank shall ask to withdraw collateral and substitute therefor other collateral against Federal reserve notes, the Federal Reserve Agent shall examine said substitute collateral and pass upon it in exactly the same way as if it were collateral for original issue of Federal reserve notes. If approving the collateral, he may make the exchange, reporting the fact at once to the Federal Reserve Board, using Form B.D. 28-3.

(21) When Federal reserve notes have been returned by the Reserve Bank to which issued, and the collateral and other security returned to the bank, said notes shall be held by the Federal Reserve Agent and shall be reissued only on the same terms as an original issue, and with the use of the same forms. All notes so returned by Reserve Banks shall be reported at once to the Federal Reserve Board.

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December 8, 1914.

The members of the Federal Reserve Board, sitting as a committee this morning, listened to a discussion presented by representatives of Trust Companies, Savings Banks and State Banks, members of American Bankers Association, with reference to the conditions under which institutions holding State charters may be permitted to enter the Federal Reserve System.

Those present included Messrs. Hamlin, Williams, Harding, Warburg, Delano and Miller of the Federal Reserve Board, and the following bankers:

W. H. McCarter, President, Fidelity Trust Co., Newark, N. J.
John W. Platten, President, United States Mortgage & Trust Co., New York City.
Oliver C. Fuller, President, Wisconsin Trust Co., Milwaukee, Wis.
A. A. Jackson, Vice-President, Girard Trust Co., Philadelphia, Pa.
John H. Mason, Vice-President, Commercial Trust Co., Philadelphia, Pennsylvania.
B. F. Saul, President, Home Savings Bank, Washington, D. C.
Geo. E. Lawson, Vice-President, Peoples State Bank, Detroit, Mich.

A Statement embracing the views of the bankers was presented to the Board, as follows:

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December 8, 1914.

STATEMENT FOR THE PRESS.

The representatives of the banking institutions who are present to-day desire to express to your associates of the Federal Reserve Board their appreciation of the courtesy extended to them in permitting them to appear before you and of the efforts which have been made by your Board to meet the convenience of our committee in the postponement of the meeting from December 2nd until to-day.

While we are appreciative of your efforts in this direction, we nevertheless feel that sufficient time has not elapsed since the appointment of our committee by the president of the American Bankers Association, said committee being appointed only on November 9, to have given proper and full consideration to the weighty problems involved in this subject and to have arrived at any conclusion in the settlement of the problems.

The resolution passed by the American Bankers Association, and under which this committee is acting, had for its object the suggestion of such change or changes in the Federal Reserve Act as would permit state chartered institutions to enter the System and, as before stated and for the reasons given, the committee has been unable to offer any

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suggestions to the purpose for which they were appointed, and if, in offering some suggestions as to the rules and regulations to be promulgated by the Federal Reserve Board, they have strayed afield from the purpose of their appointment, they would plead their desire of full co-operation with the Government in the furthering of the banking interests of the country by doing everything in their power to assist the Federal Reserve Board in the determination of the problems with which they are now confronted.

While the Trust Companies have given a great deal of consideration involving the subject, frankly we are compelled to admit, for the reasons outlined in the beginning of my remarks, viz: the short time we have had between the date of our appointment and the date of this meeting, that we have been unable to arrive at any conclusion among ourselves by which we could make any suggestions to you looking toward such amendments as might be made to the Act which would encourage Trust Companies to enter the System.

Since, however, it is the intention of the Federal Reserve Board to promulgate certain rules and regulations, it may not be inappropriate to bring to your attention one or two thoughts which have occurred to us and which we would like to suggest to you for your consideration.

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POWERS AND RESTRICTIONS.

Fourth. "State banks and trust companies may continue to exercise those banking or trust company powers granted them by their state charters when such powers are not in conflict with the limitations imposed by the Federal Reserve Act or the regulations of the Board. No power however granted by a state charter which is not customarily exercised by a bank or trust company and which is not incident to the business of a bank or trust company shall be exercised by any association (incorporated under the laws of any State) which becomes a member of the Federal Reserve System. The Reserve Board reserves to itself the determination as to whether these unusual powers are admissible and consistent. The applying bank must file with its application, as an exhibit, its statement showing powers granted to it by its state charter and those powers which it desires and intends to exercise."

It occurs to us that it may be difficult to determine what are the powers usually exercised by trust companies. Their powers are enumerated in the several state statutes under which they are incorporated. There is considerable difference between the powers granted such companies by the different state laws. In addition to this some of the trust companies are operating under private charters and exercising not only the powers given under such charters, but also the powers given

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under the general statutes.

Under these conditions an applying trust company will be confronted with the necessity of immediately determining what powers it would like to exercise in the future and possibly of being compelled to discard some of the powers granted by its charter because the Federal Reserve Board, which is a continuing power, might be of the opinion that some of these powers not customarily exercised were inconsistent with the Federal Reserve System and therefore inadmissible.

Our disposition being in every respect that of supporting the Federal Reserve Board and the recent banking legislation we had thought possibly, after an opportunity had been afforded to the trust companies of watching the operations of the Act as applied to National Banks, that later on any state chartered institution would be able to enter the System and, after a fair trial of the same, if it so desired, might retire therefrom. As the law now reads this cannot be done. The Federal Reserve Act opens the door for voluntary entry of state institutions, but does not permit voluntary exit except through liquidation.

Sec. 10. "The Federal Reserve Board will from time to time make such amendments and adopt and publish such additional regulations and by-laws as may be deemed necessary and advisable."

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This regulation seems to us to contain elements of great danger to state chartered institutions entering the System and to impose hardships upon them which are not imposed upon national banks, for the duties, the privileges, and the limitations as applied to national banks in the Federal Reserve Act are defined and prescribed, while under this regulation a future Federal Reserve Board may prescribe regulations for the conduct and management of state chartered institutions which may be difficult to comply with, and the above mentioned class of institutions would have no remedy or power to escape their enforcement except again by liquidation.

In offering these comments, we trust that you will realize that, for the reasons I have already stated, they merely represent the personal views of the members of the legislation committee of the Trust Company Section.

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WARRANTS.

Regulation No..... Covering Sec. 14 Clause (b)

This clause reads as follows:

"Every Federal reserve bank shall have power:

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

The power to buy and sell bonds and notes of the United States will be treated in a separate regulation.

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

In order to be eligible for purchase by a Federal Reserve Bank, "warrants" must be issued

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First: In anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by a "municipality"; and the taxes or assured revenues, against which such "warrants" have been issued, must be due and payable on or before the date of maturity of such "warrants",

Taxes shall be considered as due and payable on the last day on which they may be paid without penalty.

Second: By a "municipality" which has been in existence for a period of no less than ten years and which for a period of no less than ten years previous to the purchase has not defaulted in the payment of any part of either principal or interest of any funded or other debt authorized to be contracted by it, and whose net funded indebtedness does not exceed ten per centum of the valuation of its taxable property, to be ascertained by the last preceding valuation of property for the assessment of taxes.

In computing such "net" funded indebtedness, funded debt incurred for the acquisition of self-supporting property - such as water works, docks, electric plants, transportation facilities, etc. - may be deducted to the extent that such funded debt actually is self-supporting.

Third: No Federal Reserve Bank shall be permitted to purchase and hold an amount in excess of 25% of the total amount of "warrants" outstanding at any one time issued under the provisions of Sec. 14 (b) and actually sold by a "municipality".

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Fourth: The aggregate amount invested by any Federal Reserve Bank in "warrants" shall not exceed a sum equal to ten per centum of the deposits of its member banks except with the approval of the Federal Reserve Board.

Except with the approval of the Federal Reserve Board the aggregate amount which may be invested by any Federal Reserve Bank in "warrants" of any single municipality shall be limited as follows:

5% of Deposits in warrants of a municipality of 50,000 polulation or over

3% of Deposits in warrants of a municipality of over 30,000 population but less than 50,000

1% of Deposits in warrants of a municipality of 30,000 population or less.

Where the polulation of a municipality cannot be exactly determined, the Board will give special rulings.

This regulation is subject to such modification as the Board may deem proper from time to time.

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In prescribing the above regulations the Federal Reserve Board has been guided by the principle that it is the foremost object of the Federal Reserve Act to provide for a banking machinery which responds to the ebb and flow of commerce and trade. Investments of Federal Reserve Banks must, therefore, primarily be made in commercial and banking paper.

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Accordingly purchases of warrants by Federal Reserve Banks should normally be restricted to a small proportion of the aggregate investments, and limits should be exceeded only when general banking policy renders it advisable. In any and all cases the interest of Federal Reserve Banks must be considered first in making such investments and not that of municipalities desiring to sell their obligations.

The Board was guided by this point of view when adding the regulation that Federal Reserve Banks may invest only in 25% of any outstanding issue of warrants. Federal Reserve Banks ought not to be used as ready instruments created for the purpose of financing community requirements.

In order to preserve the highest degree of liquidity of Federal Reserve Banks, investments should be made by preference in such warrants as command a wide market, thus enabling the Federal Reserve Banks to dispose of these warrants whenever it becomes desirable to reinvest in commercial paper.

The regulation prescribing that only warrants be bought offering a definite assurance that the taxes and revenues will be actually in hand before maturity, is in keeping with the general policy of the Board of restricting the Federal Reserve Banks as far as possible to investments which are of short maturity and self liquidating.

12/10/14.

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REGULATIONS RELATIVE TO STATE BANKS AND TRUST COMPANIES SUBSCRIBING FOR STOCK OF FEDERAL RESERVE BANKS.

1. The Federal Reserve Act provides that a State bank or a trust company wishing to join the Federal Reserve System may do so, either:

   (a) By changing its charter for a national bank charter, in which case it should make application to the Comptroller of the Currency for permission to convert itself into a national banking association.

   (b) By retaining its State charter, in which case it is required to conduct its business under certain statutory limitations and conform with such rules and regulations as the Federal Reserve Board may prescribe.

2. These regulations deal with the admission to the System of State banks and trust companies which wish to retain their State charters, and set forth the statutory limitations and the rules, regulations and by-laws under which the Federal Reserve Board will permit State banks and trust companies to become stockholders of Federal reserve banks.

STATUTORY LIMITATIONS.

3. Attention is called to those sections of the Federal Reserve Act and of the Revised Statutes of the United States which are made applicable to State banks, banking associations and trust companies as members of the Federal Reserve System. These provisions of law are printed in full in the circular which accompanies these regulations and should be carefully examined by the applying bank.

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APPLICATIONS FOR ADMISSION.

4. A State bank or trust company which desires admission to the Federal Reserve System will be required:

(a) Under authorization of its Directors, to make application to the Federal Reserve Board, through the Chairman of the Federal reserve bank in the district, to subscribe for an amount of stock in such Federal reserve bank equal at par to 6% of its capital and surplus.

(b) To make a statement of its condition on a form prepared by the Federal Reserve Board, accompanied by a certificate of not less than_____of its Directors that in their opinion the assets are actually worth at least the values at which they appear in such statement.

(c) To furnish a certified copy of its charter and any amendments thereto, together with a summary thereof showing (1) those powers which it is now exercising and desires to continue to exercise; (2) those powers which it is not exercising but may desire to exercise in the future; (3) those powers it is not now exercising and will engage not exercise in the future.

EXAMINATIONS.

5. The Federal Reserve Board, in conjunction with the Federal reserve bank of the district, either through the local State Banking Department, or otherwise, will cause an examination to be made of the applying bank, after which the Federal reserve bank will forward the application to the Federal Reserve Board, with a statement of the opinion of the Governor and the Federal Reserve Agent, upon the following points:

(a) Whether its capital and surplus are unimpaired.

(b) Whether its management is satisfactory.

(c) Concerning the character of its deposits.

(d) Concerning the character of its loans and investments, especially whether they are, when considered in connection with the character of its deposits, of a sufficiently liquid nature to conform to sound local banking practice within the district.

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DECISION OF FEDERAL RESERVE BOARD.

It is the duty of the Federal Reserve Board in admitting State banks to membership to consider carefully all factors relating to or affecting the eligibility of such banks. The statute prescribes , as a condition of continuing membership, a strict compliance with the provisions of the Act and with the regulations of the Board. The application of every State bank involves a voluntary act on the part of the directors of the applying bank, and a voluntary submission to the Federal laws and regulations made pursuant thereof, by such banks when such submission is not in contravention of State law.

The only corporations eligible to membership are State banks, banking associations, trust companies, and national banks. It must appear to the satisfaction of the Board, therefore, that the applying corporation is engaged in the business of a State bank, banking association or trust company, and that only those powers which may be exercised under the laws of the State in which such State bank, banking association, or trust company is located, are being exercised and enjoyed by the applying bank.

In determining, therefore, whether a bank, banking association or trust company shall be admitted to membership in a Federal reserve bank, the condition and general character of its business, as well as any unusual charter powers it may possess not incident to the business of such bank, banking association or trust company, will be considered in each case by the Federal Reserve Board; and only those banks will be admitted whose charter powers are restricted to the business of a State bank, banking association or trust company within the meaning of the statutes of the State in which such bank is incorporated or organized.

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No. 4.

GENERAL PROVISIONS.

6. Upon the acceptance of an application, payments of instalments on the subscription to capital stock of the Federal reserve bank, and transfers of reserve, shall be made in accordance with law.

State banks and trust companies as members of the Federal reserve system, will be entitled to all the privileges of member banks and will be subject to all the provisions of the Federal Reserve Act which relate to member banks under the terms of the Act approved December 23, 1913, and known as the Federal Reserve Act.

The character of loans and investments made by State banks and trust companies which apply for membership in the Federal reserve system, must be made to conform within a reasonable time to the provisions of the Federal Reserve Act and other acts made applicable to such banks as members of the system.

All banks applying will be required to give proper assurances that they will adjust in due course, and within a reasonable time, all loans and investments so as to conform in all respects to the restrictions imposed by law.

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(Third draft)

Regulation No. 7 a.

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FEDERAL RESERVE BOARD.

Washington, D. C.,_____

Section 19 of the Federal Reserve Act provides in part as follows:

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

It is not the purpose of the Board to countenance or permit the reduction of reserves to 5% on deposits that are demand deposits, within the meaning of Section 19 of the Federal Reserve Act, upon the theory that they become time deposits by virtue of some blanket provision in the by-laws of a bank, stipulating that in times of emergency 30 days' notice of withdrawal may be required of deposits which are ordinarily subject to check without restriction.

The Board therefore deems it advisable to amplify Regulation No. 7, and to define in greater detail "time deposits", including "savings accounts" and "certificates of deposit", which are subject to not less than 30 days' notice before payment.

TIME DEPOSITS.

The term "time deposits" is interpreted to include such "savings accounts" and "certificates of deposit" as are subject to not less than 30 days' notice before payment, as well as those deposits which can not be checked upon or withdrawn by the depositor in advance of a certain specified time,-in no case less than 30 days-by virtue of a written contract entered into with the depositor at the time the deposit was made, and which are therefore not payable within 30 days. Any agreement,written or oral, entered into by a member bank not to enforce the terms of such contract or any payments,

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prior to the agreed date, of checks against a deposit (other than savings accounts and certificates of deposit hereinafter referred to), reported as or treated by a member bank as a time deposit in calculating its reserve, shall be construed as vitiating the contract, not only with respect to such deposit, but as to all deposits of that class; and any member bank reporting as time deposits any deposits on which it does not as a matter of fact, except as hereinafter specified, require not less than 30 days' notice before withdrawal, may be subject to the penalties prescribed by Section 5209 of the Revised Statutes of the United States (See page 62 for Section 5209)

SAVINGS ACCOUNTS.

The term "savings accounts" shall be held to include those interest-bearing accounts which are carried with the bank under written agreement on the part of the bank to pay a specific rate of interest, which rate is to be paid to all other depositors having similar accounts, - and where the depositor is required to present his passbook with each check drawn. Where this requirement is strictly observed, savings accounts are herein defined which are subject to not less than 30 days' notice before withdrawal by virtue of written contract entered into with the depositor, may be classed as time deposits although notice of withdrawal is not required in ordinary course of business; but in no case shall savings accounts be held to include any checking accounts where presentation of the passbook with the check at time of payment is not required. In States having statutes limiting the amount that a savings bank may receive from any one depositor, no member bank will be permitted to classify as a savings account, any account showing a balance in excess of such limit, and in no case shall an account showing a balance of more than $5,000 be held to be a savings account. In the case of State banks and trust companies

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located in States whose laws require that funds accuring from savings accounts shall be invested in any particular class of securities, only those accounts whose balances are so invested and handled to comply with the requirements of the State laws shall be held to be savings accounts within the meaning of this Act.

CERTIFICATES OF DEPOSIT.

A "certificate of deposit" is defined as an instrument evidencing the deposit with a bank of a certain specified amount payable to the payee named in the face of the instrument or his order on demand, or on a certain specified date, or after the lapse of a certain specified time after date of the instrument, either with or without interest, an essential feature of the instrument being that the deposit evidenced thereby is not subject to check, but is payable only upon surrender of the certificate properly endorsed. Only such certificates of deposit as clearly show on their face that they are payable at a time not less than 30 days after the date upon which the reserve is calculated shall be deemed to be time deposits within the meaning of this Act.

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ACCEPTANCES.

REGULATION NO. 1.

Non-member banks and trust companies, and private banking firms desiring to have their acceptances made eligible for discount with Federal Reserve Banks must file an application with the Federal Reserve Bank of their district. The Federal Reserve Bank shall forward the application to the Federal Reserve Board with a report and recommendation. In case the Federal Reserve Board, upon the recommendation of the Federal Reserve Bank, approves the application, the name of the applicant shall be entered in a register to be kept by the Federal Reserve Board and all Federal Reserve Banks shall be notified that the name has been so registered. After receipt of this notification, the Federal Reserve Banks shall be permitted to purchase at their rate fixed for bank acceptances, the acceptances of such applicants, provided: 1. that the acceptance mature within three months from the date of the purchase of said acceptance; 2. that such acceptance be drawn to finance transactions involving the importation or exportation of goods and must bear on the face of the bill some reference to such transaction; 3. that it bear the signatures of at least three separate and distinct parties, viz: the acceptor, the drawer, and no less than one indorser. One indorser must be a member bank, or a registered non-member bank or trust company, or a registered private banking firm. Every Federal Reserve Bank shall, at least once a year, send to the Federal Reserve Board a report concerning each bank, trust company or banking firm admitted to the

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acceptance register. The Federal Reserve Board may at any time withdraw such name or names from the register and upon receipt of a notification that such name has been withdrawn, the permission to Federal reserve banks to purchase the acceptance of a firm so withdrawn, shall be considered as cancelled.

Every Federal reserve bank shall send a weekly report to the Federal Reserve Board stating in detail all purchases of bank acceptances.

Regulation No. 2.

Acceptances of member banks in order to be eligible for rediscount by Federal reserve banks must bear the signatures of at least three separate and distinct parties, viz: the acceptor, the drawer and no less than one endorser. One endorser must be a member bank or a registered non-member bank or trust company or a registered private banking firm.

Regulation No. 3.

Member banks shall be required to specify in the regular statements to their Federal reserve banks the aggregate amount of bills accepted by them and outstanding at the time and the aggregate amount of bank acceptances endorsed by them outstanding at the time. Non-member banks and trust companies admitted to the acceptance register shall obligate themselves to make a similar statement to the Federal reserve bank of their district at the end of each month. Private banking firms admitted to the acceptance register shall, at the end of each month, state to the

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Federal reserve bank of their district the aggregate amount of bills accepted by them and at the time outstanding.

Regulation No. 4.

Only such non-member banks and trust companies or accepting discount or finance corporations shall be admitted to the acceptance register as have an aggregate unimpaired capital and surplus of no less than $1,000,000, and only such private banking firms shall be admitted to the acceptance register as furnish a statement under oath to the Federal reserve bank of their district that their unimpaired, paid in capital is no less than $2,000,000.

P. M. W.
12-7-14.

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Fifth draft.

REGULATION No. 7-a. F E D E R A L R E S E R V E B O A R D

Washington, D. C., _____,

Section 19 of the Federal Reserve Act provides in part as follows:

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

It is not the purpose of the Board to countenance or permit the reduction of reserves to 5% on deposits that it construes to be demand deposits within the meaning of Section 19 of the Federal Reserve Act, upon any theory that such deposits become time deposits by virtue of a blanket provision in the by-laws of a bank stipulating that in time of emergency 30 days notice of withdrawal may be required as to deposits which are ordinarily subject to check without restriction.

The Board therefore deems it advisable to amplify Regulation No. 7, and to define in greater detail

1: Time deposits, open accounts,

2: Savings Accounts,

3: Certificates of Deposit,

1. TIME DEPOSITS, OPEN ACCOUNTS.

Under this head are included all accounts not evidenced by certificates of deposit or savings passbooks which may under agreement be checked upon or withdrawn only upon written notice given by the depositor a certain specified number of days in advance, in no case less than 30 days, such an agreement to be in the form of a written contract entered into with the depositor at the time the deposit is made. Where it is provided that a deposit may be withdrawn by check

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within 30 days, such deposit will be held to be a demand deposit irrespective of the fact that the bank has the right by written contract or otherwise to require a withdrawal notice of more than 30 days. In other words, no deposit shall be deemed a time deposit unless it be withdrawable only at a date or after a period more than 30 days subsequent to the date as of which the reserve is to be calculated.

2. SAVINGS ACCOUNTS.

Savings accounts are held to include all interest bearing accounts carried under written contracts, which contracts may appear on the face or back of signature cards signed by the depositor, or may be printed in the passbook issued to the depositor, under terms of which contract the depositor is required to present his passbook with each check drawn, and such contracts to contain a clause subjecting the account to at least 30 days notice, at the option of the bank, before withdrawal. No account shall be deemed a savings account if the presentation of the passbook is not required at the time of the payment of a check or withdrawal of the deposit.

3. TIME CERTIFICATES OF DEPOSIT.

Time certificates of deposit are defined as instruments evidencing a deposit with a bank of a certain specified amount repayable to the payee named in the face of the instrument, either with or without interest, on a certain specified date or after the lapse of a certain specified time after date of the instrument (such time or date being not less than 30 days after the date as of which the reserve is calculated). No deposit which is subject to check or which may be repaid in whole or in part without the surrender of the certificate properly endorsed shall be deemed to be a certificate of deposit.

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The Governors of the Federal Reserve Banks have expressed the desire that the operation of Regulation No. 4, which under its terms was to go into effect on January 15th, should be deferred for the present. This regulation relates to statements that member banks would be required to receive from their customers in the future, and the unanimous opinion expressed by the Governors was that it would be desirable and helpful particularly to the country banks in many districts to allow ample time for both member banks and their customers to adjust their methods to these new requirements.

The Board has, therefore, decided that Regulation No. 4 shall not go into effect on January 15th, but that it will be held in abeyance for several months. A definite announcement will be made in due course. It is the desire of the Board to facilitate the operations of the Reserve Banks in any way consistent with the law.

12-19-14

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The following is suggested as an outline of principles that should be followed by Federal Reserve Banks in certain cases in dealing with applications of member banks for rediscounts:

(1) Where a bank applying for rediscounts is found to be in an extended condition, the question should be definitely raised as to how far the funds requested are to be used in the liquidation of the outstanding obligations of the institution, and how far they are being called for to finance new transactions of the same kind that have already led to the extended condition of the bank. In cases where funds are desired for the liquidation of indebtedness, the accommodation may well be granted; in any other case they should be declined.

(2) In cases where a presumably sound bank offers doubtful or questionable paper, such paper should be rejected without hesitation regardless of the question as to whether the bank's endorsement would in the last analysis make it good.

(3) In cases where the paper offered is of such character as to comply with the regulations laid down by the Board, but does not appear to possess such strength as to altogether satisfy the directors as to its desirability, no objection would be made to their requiring the applying bank to fortify its endorsement of such paper by approved collateral deposited under a collateral agreement with the reserve bank.

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Washington, D. C.

December 19, 1914.

Secretary McAdoo today made public the following opinion from the Attorney General:

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OFFICE OF THE ATTORNEY GENERAL

Washington, D. C.

The Honorable

The Secretary of the Treasury,

Washington, D. C.

Sir:

I have the honor to acknowledge your letter of October 29th, 1914, wherein you request my opinion (a) whether accounts of moneys derived from the semi-annual assessment to be levied on Federal Reserve Banks by the Federal Reserve Board, are subject to audit by one of the auditors of the Treasury Department, and (b) as to the status of the Federal Reserve Board, particularly with reference to the Treasury Department.

Section 10 of the "Federal Reserve Act" of December 23, 1913 (the act authorizing the assessment), provides:

> "The Federal Reserve Board shall have power to levy semi-annually, upon the Federal Reserve Banks, in proportion to their capital stock and surplus, an assessment sufficient to pay its estimated expenses and the salaries of its members and employees for the half year succeeding the levy of such assessment, together with any deficit carried forward from the preceding half year."

The answer to your first question depends on whether the moneys so levied by the Federal Reserve Board are, when received, "public moneys." If so, they are clearly to be audited under Sections 7 and 10 of the Act of July 31, 1894, (28 Stat. 207) either by the auditor provided for in the first paragraph of said Section 7 or by the audi-

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tor provided in the fifth paragraph, such paragraphs (so far as material) reading as follows:

> FIRST. "The Auditor for the Treasury Department shall receive and examine all accounts of salaries and incidental expenses of the office of the Secretary of the Treasury and all bureaus and offices under his direction, all accounts relating to . . . and all other business within the jurisdiction of the Department of the Treasury and certify the balances arising thereon to the Division of Bookkeeping and Warrants."
>
> FIFTH. "The Auditor for the State and other departments shall receive and examine all accounts of . . . and accounts of all boards, commissions and establishments of the Government not within the jurisdiction of any of the Executive Departments. He shall certify the balances arising thereon to the Division of Bookkeeping and Warrants."

Section 10 (so far as material), provides for a Division of Bookkeeping and Warrants, and that:

> "Upon the books of this division shall be kept all accounts of receipts and expenditures of public money" etc.

Reference is also to be made to the Act of February 19, 1897 (29 Stat. 550), reading (so far as material) as follows:

> "All books, papers and other matters relating to the office or accounts of . . . commissions, boards and establishments of the Government in the District of Columbia, shall at all times be subject to inspection and examination by the Comptroller of the Treasury and the Auditor of the Treasury authorized to settle such accounts, or by the duly authorized agents of either of said officials."

(This statute plainly applying to boards etc., <u>located</u> within the District of Columbia, rather than to boards of the District Government; and the Federal Reserve Board being located within the District.)

I am of opinion that moneys received by the Federal Reserve Board, under Section 10 of the Act of December 23, 1913, are "public moneys" within the meaning of these auditing statutes, for the following reasons, among others:

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(1) The assessments are levied by a board whose members in respect to appointment, tenure, duties, and compensation meet all requirements of the definition "public officers" and "officers of the United States".

(2) The assessments are levied by such officers pursuant to the provision of a Federal statute and are devoted to the payment of official salaries and the expenses of this official board.

(3) These moneys after collection, are no longer the property of the paying banks, and must be viewed as moneys belonging to the United States, and therefore public moneys as defined by the Supreme Court of the United States in Branch v. United States, 100 U. S. 673. In United States v. Bromley 12 How. 88, it was held, that postal collections from stamp sales are public revenues:

> "The revenue of the Post Office Department being raised by a tax on mailable matter conveyed in the mail and which is disbursed in the public service, is as much a part of the income of the Government as moneys collected for duties on imports."

The analogy is marked for the reason that in like manner as the money assessed by the Federal Reserve Board is for the special purpose of meeting the salaries and expenses of the Board, so the use of the postal collections is confined to sustaining the specific service by and in which they are collected.

(4) Other provisions of the Federal Reserve Act (Secs.11-c and 16), dealing with interest charges, taxes and penalties, can only be satisfied by deposit in the Treasury of the levies, taxes and penalties so imposed,

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and there seems to be no logical ground for distinction between such assessments and the ones in question. The idea of necessary public control is also strengthened by the requirements of Rev. Stat. Sec. 3639.

The moneys received by the Federal Reserve Board under Section 10 of the Act of December 23, 1913, being thus, in my opinion, public moneys and consequently subject to audit by one of the auditors of the Treasury Department, the question is then directly presented under which paragraph of the Act of July 31, 1894, supra, the audit is to be made. This involves the further question on which you have asked my opinion: namely, whether the Federal Reserve Board is an independent board, commission or Government establishment or whether it is a bureau, office or division or otherwise a part of the Treasury Department.

That the Federal Reserve Board is a "board" or "establishment" of the Government within the meaning and intent of those words as used in the Fifth Paragraph of Section 7 of the Act of July 31, 1894, is plain from the provisions of the Federal Reserve Act and the explanation of the status of the Board contained in the Reports accompanying the original bills in Congress. This conclusion is sustained by reason and analogy, when reference is had to the considerable number of boards or establishments of far less general or National scope which have been so esteemed and uniformly treated. (See Report of Joint Commission to Inquire into Executive Departments, October 9, 1893. House Reports, 1st Session, 53rd Congress, Report No. 88).

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Consideration of the history of the Federal Reserve Bank Act, of the general scheme of the whole act, of the functions to be performed by the Federal Reserve Board and of the method of their performance, leads me to the clear opinion that the Board is an independent board or government establishment.

The Federal Reserve Board is not merely a supervisory, but is a distinctly administrative board with extensive powers. It is described as follows in the Report of the Committee on Banking and Currency to the House of Representatives (63d Congress, 1st Sess., Report No.69):

p.16. "In order that these banks may be effectively inspected and in order that they may pursue a banking policy which shall be uniform and harmonious for the country as a whole, the committee propos es a general board of management intrusted with the power to overlook and direct the general functions of the banks referred to. To this it assigns the title of "The Federal Reserve Board."

. . . . . .

p.18. "The only factor of centralization which has been provided in the committee's plan is found in the Federal Reserve Board, which is to be a strictly Government organization created for the purpose of inspecting existing banking institutions and of regulating relationships between Federal reserve banks and between them and the Government itself." .....

p.42. "Section 11. In this section provision has been made for the creation of a general board of control acting on behalf of the National Government....."

The report of Senator Owen from the Senate Committee on Banking and Currency (63d Congress, 1st Session, Report 133,part 2) says merely:

"The Federal Reserve Board consisting of the Secretary of the Treasury and six members appointed by the President of the United States and confirmed by the Senate for terms of six years, are given the following powers: "(Here follows an enumeration of powers.)

The broad functions outlined in these Reports are assigned to the Board in twelve subdivisions of Section 11 of the Act giving to it certain powers and authority, and in various other sections containing

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specific grants of authority to exercise about forty other powers. Moreover, in subdivision (i) of Section 11 the all-embracing requirement appears that "said board shall perform the duties, functions or service specified in this Act, and make all rules and regulations necessary to enable said board effectively to perform the same."

The Act, further, contains no express provision that the Federal Reserve Board shall be considered as a bureau, division or office of the Treasury Department -- a significant omission in view of the fact that Congress had under consideration a Bureau of that Department when in Section 16 it amended the Revised Statutes relative to that "bureau" of which the Comptroller of the Currency was the "chief officer": and the provision in Section 10 that "the Secretary of the Treasury may assign offices in the Department of the Treasury for the use of the Federal Reserve Board" (a provision added to the House Bill by the Senate Committee) would be highly superfluous if the Board were a bureau of that Department for which the Secretary already possessed complete authority to assign offices in his own departmental buildings.

The history of the bill develops the following facts of significance.

In Section 11 of H. R. 7837 (Section 10 of the Act), it is provided:

> "The manager of the Federal Reserve Board, subject to the supervision of the Secretary of the Treasury and Federal Reserve Board, shall be the executive officer of the Federal Reserve Board."

This clearly contemplated that the Secretary of the Treasury and the Federal Reserve Board were distinct entities.

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In the Act as passed, (Section 10) the supervision of the Secretary of the Treasury is stricken out, leaving the Governor(Manager) subject only to supervision of the Board.

In Section 16 of H. R. 7837 (Section 16 of the Act) it is provided:

> "The Secretary of the Treasury shall subject to the approval of the Federal Reserve Board from time to time apportion the funds of the Government among the said Federal reserve banks, distributing them as far as practicable equitably between different sections...."

This also clearly contemplated the Secretary and the Board as co-ordinate officials. The whole provision was stricken from the Act as passed but nothing was substituted for it.

In Section 11 of H. R. 7837 (Section 10 of the Act) the Comptroller of the Currency was to perform his duties "under the general direction of the Secretary of the Treasury acting as chairman of the Federal Reserve Board.

In the Act as passed the words "acting as chairman of the Federal Reserve Board" were stricken out, showing an intention to distinguish clearly between placing the Comptroller under the Secretary as head of the Treasury Department and the Secretary as ex officio chairman of the Board.

The most significant change made in H. R. 7837 by the Act as passed was the insertion, in Section 10 of the Act, of the following clause:

> "Nothing in this Act contained shall be construed as taking away any powers heretofore vested by law in the Secretary of the Treasury which relate to the supervision, management, and control of the Treasury Department and bureaus under such department, and whenever any power vested by this Act in the Federal Reserve Board or the Federal reserve agent appears to conflict with the powers of the Secretary of the Treasury, such powers shall be exercised subject to the supervision and control of the Secretary."

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It is evident that, while the purpose of this clause was, amongst other things, to insure the preservation and supremacy of all existing powers of the Secretary of the Treasury in all cases where it might be claimed that such powers overlapped, or conflicted with those of the Federal Reserve Board, nevertheless by this very provision the Act clearly recognized the existence of powers of the Board independent of the Secretary in cases where no such conflict existed.

Very respectfully,

(Signed) T. W. Gregory

Attorney General.

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EXAMINATION OF STATE BANKS AND TRUST COMPANIES APPLYING FOR MEMBERSHIP - FEDERAL RESERVE SYSTEM.

Name of Bank_____

Information Desired.

1. Character of business in community in which your institution is located.

2. Character of business of Bank.

3. State law limitations -

   A. Loans to any one firm, corporation or individual - secured and unsecured.
   B. Loans secured by Real Estate Mortgages or other real estate collateral
   C. Investments.

4. Date of last examination by State authorities

   A. Were trust investments and securities examined?

5. Date of last examination by Directors.

6. Copy of Daily Statement.

7. Memorandum of material changes since (insert date application report)

8. Real Estate Loans and Investments.

   A. Loans secured by unencumbered farm lands

      1. Up to what extent of value is money advanced - How is value determined.

   B. Loans secured by other Real Estate

      1. Is collateral held-subject to prior liens?

      2. Are mortgages on productive or non-productive properties?

      3. Give list of loans of ($ or more) secured by

         a. First mortgages.(Extent prior lien)) Estimated value of pro-
         b. Second mortgages ") perties- when and by
         c. Deeds to Real Estate Properties ") whom appraised.
         d. Stocks and bonds issued by real estate corporations or based upon other real estate securities.
         e. Loans to individuals connected with real estate trading corporations with description of collateral, if any.

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C. Real Estate Owned - give list showing

1. Prior mortgages. 2, Assessed valuation. 3. Income. 4. Taxes - Expenses - Interest. 5. Estimated value. 6. when and by whom appraised. 7 How acquired?

9. Loans and Discounts.

A. Secured by Collateral other than Real Estate and unsecured Loans and Discounts.

1. What is the general character of collateral held.

2. List of loans secured by Bank stock with details

3. Give list of loans to any one individual, firm or corporation in excess of (insert figures equal to 10% of capital and surplus)

4. Give list of loans over ($) with details. Name of Borrower-Business-Address of borrower-Amount of loan- Approximate deposit balance.

5. Give list of loans, maturing after one year

B. Unsecured Demand Loans

1. Character of loans - Amount of loans upon which no interest has been paid for one year or more, with a description of collateral, if any.

C. Doubtful Loans

1. Amount of notes or other loans in default six months or more and which are not properly secured or in process of collection - Give list with details, items over $

D. Overdrafts - Secured and unsecured. Details

10. Investments.

A. Give list of investments in detail, showing securities - rate of interest or dividend - Par value - Book value and valuation based upon current or last available quotations.

B. List of investments in default.

C. Provisions for depreciations.

D. Are book values adjusted periodically to agree with current valuations.

11. Deposits.

A. Does the item on report "Certificates of Deposit time" include any sum or sums due to banks - bankers or trust companies, if so please give particulars.

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B. When were ledgers last proven.

12. Notes and bills rediscounted, Bills Payable and Certificates of deposit representing money borrowed -

A. What is the present amount of indebtedness.

B. What assets have been pledged as security for indebtedness.

13. Contingent Liabilities -

A. On bills rediscounted or endorsed. - B. Guarantees. C. All other - give particulars. D. Notes and securities pledged or sold with agreement to repurchase.

14. Assets pledged as security for deposits or other purpose except money borrowed.

A. Give particulars.

15. Has the Trust Company or Bank any contingent liability? If so please give full particulars.

16. Directors Liabilities -

A. Please give a memorandum of the

1. Business firm and corporation affiliations of officers and Directors.

2. Direct and indirect liabilities of officers and directors.

3. Loans of ($ or over) made to corporations which are owned or controlled by officers or directors of the banking institutions.

17. Examiners Opinion.

A. Is the institution solvent?

B. Is business conducted strictly in accordance with the provisions of the law (State Law)

C. Is the management of the institution competent?

D. Do you consider the loan policy safe and conservative?

E. Are there any unsafe or unsound tendencies apparent?

F. Has there been an increase in undesirable assets during the past year?

G. Do directors give proper time and attention to the affairs of the institution?

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H. Is the stock control of institution held by any one person or group?

I. What is the policy of the institution in granting loans, to officers and directors or to enterprises which they control or are interested in?

K. Copy of text of report of last examination.

12/21/14

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EX-OFFICIO MEMBERS

WILLIAM G. McADOO
SECRETARY OF THE TREASURY
CHAIRMAN

JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

W. P. G. HARDING, GOVERNOR
PAUL M. WARBURG, VICE GOVERNOR
FREDERIC A. DELANO
ADOLPH C. MILLER
CHARLES S. HAMLIN

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY-TO
FEDERAL RESERVE BOARD

December 21, 1914.

Sir:

Answering queries raised by a number of the Reserve Bank Boards in respect to Directors' fees, etc., I am able to advise you the decisions that have been reached by the Federal Reserve Board.

1. The fee to be paid to directors' meetings is fixed at $20.00 per meeting as a maximum. Of course it is conceivable that you might have a series of meetings on consecutive days, in which case one would think that the fee would be $20.00 each day until the series of meetings were over.

2. The directors who live more than fifty miles from Federal Reserve banks receive $10.00 per day for every day they are away from home on account of attendance, from the time they start until the time they get back, assuming that their absence is entirely due to attendance upon the directors' meeting. This makes a $10.00 per day compensation in addition to the director's fee.

3. The words "necessary travelling expenses" includes hotel bills, as well as other necessary expenses of the journey and absence from ~~from~~ home of out-of-town directors during their stay in the City, if they are engaged in attending directors' meetings.

4. The ruling of the Board allows not to exceed $10.00 per meeting for attending meetings of the Executive Committee, and if, as suggested, the Executive Committee should be required to be on duty all day, or for several days, the amount of his fee would be the number of meetings held during that time multiplied by ten; i. e., this would be the maximum.

5. If the Committeeman so serving should be a non-resident, he would be entitled to reimbursement for his hotel bills and other reasonable necessary expenses while actually serving.

I have the honor to be,

Very respectfully,

Secretary.

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Tentative Circular No.

FEDERAL RESERVE BOARD.

Washington, December 22, 1914.

Bankers' Acceptances.

Bankers' acceptances, in order to be eligible for purchase by a Federal reserve bank, must bear on their face evidence that the acceptance originated in a transaction involving the importation or exportation of goods; that is to say; in an actual bona fide sale or consignment, which involves the transportation of goods from some foreign country to the United States, or from the United States to some foreign country.

Bankers' acceptances, other than those of member banks, must bear the endorsement of a member bank.

Acceptances of member banks must bear the endorsement either of a member bank, other than the accepting bank, or that of another "banker", as defined in the accompanying circular, of satisfactory standing and located in the district of the Federal reserve bank.

C. S. HAMLIN,

Governor.

H. PARKER WILLIS,

Secretary.

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97 Tentative Circular

FEDERAL RESERVE BOARD.

Washington, D. C.,
December 22, 1914.

- Subject: - The Purchase of Warrants. -

In drawing Regulation No. 10 the Federal Reserve Board has been guided by the consideration that it is the primary purpose of the Federal Reserve Act to provide a banking organization which shall be responsive to the ebb and flow of commerce and trade.

Inasmuch as investments of Federal Reserve banks' resources should primarily be restricted to commercial paper and acceptances, purchases of warrants by Federal Reserve banks should ordinarily be limited to a relatively small proportion of the aggregate of investments. This practice should be departed from only when general banking policy renders it advisable. In any and all cases the interest of the Federal Reserve banks rather than that of the municipalities desiring to sell their obligations should be the primary consideration in making such investments.

In accordance with this view the Board has limited Federal Reserve banks to 25% in their purchases of any outstanding issue of warrants.

In order to keep the assets of the Federal Reserve banks in a liquid condition investments in warrants when made should be made by preference in such as can be readily marketed in order that the Federal Reserve banks may be able to realize on them whenever it becomes desirable to enlarge their investments in commercial paper.

In limiting the Federal Reserve banks to such warrants as carry the definite assurance that the taxes and revenues will be actually in hand before maturity the Board endeavors to follow the policy of the Act in restricting the Federal Reserve banks as far as possible to investments which are of short maturity and self-liquidating.

Charles S. Hamlin
Governor.

H. Parker Willis
Secretary.

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FEDERAL RESERVE BOARD.

Washington, D. C.
December 22, 1914.

Subject: - Bankers' Acceptances.

Section 14 - Federal Reserve Act.

The Federal Reserve Board on November 10, 1914, promulgated Regulations Nos. 2 and 6, governing the conditions upon which Federal reserve banks might discount bank acceptances.

The Board hereby revokes Regulation No. 6 and substitutes therefor Regulation No.6a, hereto attached.

Under Section 14 of the Act, the Federal Reserve Board is authorized to prescribe rules and regulations under which any Federal reserve bank may "purchase and sell in the open market, at home or abroad, either from or to domestic or foreign banks, firms, corporations or individuals, cable transfers and bankers' acceptances and bills of exchange of the kinds and maturities by this Act made eligible for rediscount with or without the endorsement of a member bank."

Following the analogy of the Internal Revenue Act of October 22, 1914, which defines the word "banker", the term "bankers' acceptances" whenever used in regulations or circulars of the Federal Reserve Board shall be construed so as to include the acceptances of member banks, non-member banks, trust companies, private banking firms, persons or companies engaged in the business of accepting and discounting.

Under the said Section 14, the Federal reserve banks are given power "to establish from time to time, subject to review and determination of

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the Federal Reserve Board, rates of discount to be charged by the Federal reserve banks for each class of paper, which shall be fixed with a view of accommodating commerce and business."

Transactions in "bankers' acceptances" at rates substantially lower than those for commercial paper have already reached considerable proportions in the open market and it is necessary for the Federal reserve banks to establish discount rates covering such paper.

Acceptances covering the importation or exportation of goods have to compete with foreign acceptances in world markets, and the rates for these bankers' acceptances in the United States must be such as to enable the American banker to meet successfully his foreign competitor.

In order to meet these conditions the Board realizes that Federal reserve banks must be allowed some latitude in dealing with such acceptances.

The Federal Reserve Board, has, therefore, determined that in establishing rates for bankers' acceptances Federal reserve banks may from time to time submit to the Federal Reserve Board a maximum and a minimum rate, varying not more than 1 per centum, within the limits of which they may ask to be authorized to purchase bankers' acceptances. Within these limits the Federal reserve banks will be permitted to determine the rates at which they will deal in bankers' acceptances. The Board, however, reserves the right to modify or withdraw this privilege.

Federal reserve banks are requested to furnish to their Federal reserve agents copies of the resolutions authorizing the purchase of bankers acceptances and the limit fixed for the aggregate amount to

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be purchased of each acceptor's paper; and, in addition, a daily statement giving the total amount of all bankers' acceptances purchased, the rates at which purchased, and the names of the acceptor, drawer and endorser of every bill. The Federal Reserve Agent shall forward such copies and statements to the Federal Reserve Board.

In deciding what acceptances shall be considered satisfactory, the Federal Reserve Board must necessarily depend chiefly on the judgment of the officers and directors of the various reserve banks who are in active daily touch with the business situation of the entire district.

C. S. HAMLIN

Governor.

H. PARKER WILLIS

Secretary.

12-22-14.

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Tentative Regulation

FEDERAL RESERVE BOARD.

Washington, D. C.

December 22, 1914.

Subject: The Purchase of Warrants.

Section 14 of the Federal Reserve Act reads in part as follows:

"Every Federal reserve bank shall have power:

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

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

I. A Federal reserve bank may purchase such warrants as are issued by a "municipality"

(a) In anticipation of the collection of taxes or in anticipation of the receipt of assured revenues. The taxes or assured revenues, against which such "warrants" have been issued, must be due and payable

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on or before the date of maturity of such "warrants". For the purposes of this regulation taxes shall be considered as due and payable on the last day on which they may be paid without penalty.

(b) As the general obligations of the entire "municipality", it being intended to exclude as ineligible for purchase all such obligations as are payable from "local benefit" and "special assessment" taxes when the "municipality" at large is not directly or ultimately liable.

(c) 1- Which has been in existence for a period of ten years; 2- Which for a period of ten years previous to the purchase has not defaulted, for a period exceeding fifteen days, in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it; and

3- Whose net funded indebtedness does not exceed ten per centum of the valuation of its taxable property, to be ascertained by the last preceding valuation of property for the assessment of taxes.

As a definition of the term "net funded indebtedness" as used in I (c) -3, above, and in further explanation of 1(c)-1 and 2, relative to the term of existence of and non-default by the "municipality", the Federal Reserve Board has adopted in substance the definitions and regulations of the Board of Trustees of the Postal Savings System, which, as printed hereunder in an appendix hereto is made a part of these regulations.

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

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

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

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5% of such Deposits in "warrants" of a "municipality" of 50,000 population or over;
3% of such Deposits in "warrants" of a "municipality" of over 30,000 population but less than 50,000;
1% of such Deposits in "warrants" of a "municipality" of over 10,000 population but less than 30,000.

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

The population of a "municipality" shall be determined by the last Federal or State census. Where it cannot be exactly determined, the Board will give special rulings.

VI. Opinion of recognized Counsel on municipal issues, or of the regularly appointed Counsel of the "municipality" about the legality of the issue shall be secured and approved by Counsel for the Federal Reserve Bank in each case.

VII. This regulation is subject to such modification as the Board may deem proper from time to time.

H. Parker Willis,
Secretary.

Charles S. Hamlin,
Governor.

* * * * * * * * *

DEFINITION OF "NET FUNDED INDEBTEDNESS"

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

(1) The amount of outstanding bonds or other debt obligations made payable from current revenues.

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(2) The amount of outstanding bonds issued for the purpose of providing the inhabitants of a "municipality" with public utilities, such as water works, docks, electric plants, transportation facilities, etc.: PROVIDED, That evidence is submitted showing that the income from such utilities is sufficient for maintenance, for payment of interest on such bonds and for the accumulation of a sinking fund for their redemption.

(3) The amount of outstanding improvement bonds, issued under laws which provide for the levying of special assessments against abutting property in sufficient amounts to insure the payment of interest on the bonds and the redemption thereof: PROVIDED: That such bonds are direct obligations of the "municipality" and included in the gross indebtedness of the "municipality".

(4) The total of all sinking funds accumulated for the redemption of such gross indebtedness, except sinking funds applicable to bonds just described in (1), (2) and (3) above.

"Warrants" will be construed to comply with that part of paragraph (c) of this regulation, relative to term of existence and non-default, under the following conditions:

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

(2) "Warrants" issued by or in behalf of any "municipality" which was, subsequently to the issuance of such "warrants", wholly succeeded by a newly organized political division, whose term of existence, added to that of such original political division, or of any other po-

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litical division so succeeded, is equal to a period of ten years, will be deemed to be "warrants" of such succeeding political division: PROVIDED, That during such period none of such political divisions shall have defaulted for a period exceeding fifteen days, in the payment of any part of either principal or interest of any funded debt authorized to be contracted by it; AND PROVIDED FURTHER, That such "warrants" were assumed by such new political division under statutes and appropriate proceedings the effect of which is to make such "warrants" general obligations of such assuming political division, and payable, either directly or ultimately, without limitation to a special fund, from the proceeds of taxes levied upon all the taxable real and personal property within its territorial limits.

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

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Report of Committee in regard to

CIRCULARS, REGULATIONS AND MEMORANDA

First:

It is recommended that all circulars, when in permanent form, shall be printed and that regulations, if any, shall be appended or attached thereto. The circular portion shall be in the form of a letter dealing with principles and shall bear the signatures of the Governor and Secretary of the Board.

Second:

A standard size of page, style of heading and of the type to be used shall be prepared and the form selected strictly adhered to, embodying the following ideas:

(a) In the upper right hand corner the number of the circular shall appear;

(b) The name of the Federal Reserve Board shall appear in the center;

(c) To the right of and below this, the date of the circular;

(d) Below this (in the center) the title or subject matter; and,

(e) Lastly, the body of the circular, with appended regulations, if any, using a different size or style of type for the circular and the regulation.

Third:

Some less formal matters may be handled in mimeographed "memoranda." Furthermore, regulations or circulars may be mimeographed or printed as "tentative circulars" or "tentative regulations" with the idea of printing them after they have been adopted in final form. These "memoranda" or "tentative documents" shall be identified by numbers, keeping a separate series for "memoranda", for "circulars" and for "regulations." So far as possible, the mimeographed memoranda shall follow a definite form and style, to be agreed upon in advance; the circular in open spacing, the regulation in closer spacing or smaller type.

Fourth:

It is suggested that it may be desirable that at least some of the circulars and regulations already issued shall be re-issued so as to keep our files complete, making such

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corrections in the re-issue as may be found desirable; at the same time beginning the numbering in the new series. It may also be advisable to issue circulars in a new series each year thus, Series of 1915, but these suggestions should be the subject of future decision by the Board. It is probable that many of the circulars are only of passing interest or importance and that in the interest of compact and intelligent codification of all regulations, etc., previous rulings, shall be reconsidered and such as are still valid and pertinent, reenacted. This might be effectively done by annual revision and reenactment.

Respectfully submitted by
the Committee:

(Signed) F. A. Delano.

(Signed) H. Parker Willis.

Presented to the Federal Reserve Board at its meeting of

December_____1914 and adopted.

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PROPOSED DRAFT OF A FORM OF CIRCULAR TO BE ISSUED BY ALL FEDERAL RESERVE BANKS WITH THE AUTHORITY AND APPROVAL OF THE FEDERAL RESERVE BOARD

To Member Banks:

Section 13 of the Federal Reserve Act, which deals with the powers of Federal Reserve Banks, provides that:

> "Any Federal Reserve Bank may receive from any of its member banks * * * deposits of current funds in lawful money, National bank notes, Federal reserve notes, or checks and drafts on solvent member banks payable upon presentation."

The Federal Reserve Bank of _____announces that it is now prepared to receive from any member bank on deposit at par, subject to final payment, check drawn on any of the member banks of District No.___*, provided that each member bank availing itself of this privilege will authorize the Federal Reserve Bank of _____to charge its account with any checks drawn upon it that may be received from other member banks or from the United States, such checks to be forwarded without delay to the member bank for final payment.

Provided, however, that each member bank entering into this arrangement agrees to maintain with the Federal Reserve Bank of _____, subject to any penalty for insufficient reserves that may be imposed by the Federal Reserve Board, a balance, in addition to the member bank's legal reserve, sufficient to cover any excess of debit over credit items.

(*) Note:
The Federal Reserve Bank may wish to change this and, for the time being limit their taking of checks to those drawn on banks in reserve cities or on certain specified cities which they will designate.

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Federal Reserve Bank of St. Louis

November 19th, 1914.

My dear Governor:-

As requested, I have given consideration to the matter of discount rates to be charged by Federal reserve banks and particularly to the question of the application of State laws to such rates.

The question arises in interpreting Section 14 of the Federal Reserve Act.

Section 14, sub-section (d), in defining one of the powers of the Federal reserve banks, provided as follows:

> "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".

In interpreting this section, it is necessary to consider whether Federal reserve banks are limited in the amount of interest which may be charged and particularly whether such banks are subject to the usury laws of any State in the absence of any fixed maximum rates of interest prescribed by Congress. This involves a consideration of the questions -

First - Has Congress the constitutional right to prescribe a rate of interest to be charged by a corporation organized under an Act of Congress, which rate exceeds the statutory rate fixed by any State for persons, firms or corporations doing business within the limits of such State?

Second - If Congress has this right, may it delegate to any executive branch of the Government the right to fix such rates?

Third - If Congress fails to prescribe by statute a maximum rate of interest to be charged, will the executive branch of the Government be controlled by such State laws in fixing the interest rate to be charged?

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Considering these questions in the order named:

First - The right to establish interest rates is necessarily incident to the right to create a banking corporation since the exercise of this power may be said to be fundamentally a part of the exercise of banking powers.

The right of Congress to create a bank and to vest such corporation with the necessary powers to perform its functions, is fully considered and determined in the case of McCulloch vs Maryland, 4 Wheaton, 316. In that case Chief Justice Marshall, who delivered the opinion of the Court, affirmed the right of Congress to create the Bank of the United States, the right of the Bank of the United States to establish a branch in Maryland, as an incidental power not specifically granted by its charter, and decided definitely that the State of Maryland could not tax the branch so established on the ground that such a tax would retard, impede, burden or control the operations of the laws enacted by Congress. That is, the Court having decided that the Bank of the United States was constitutional, held that the branch which was created by the bank, "being conducive to the complete accomplishment of the object" was equally constitutional. This concedes the right of the bank to exercise powers which are properly incident to the duties of the bank. See Wheaton 4, pages 424-425 A fortiori, the right to establish interest rates, equally free from State interference, is incident to the duties of the Federal reserve banks.

Without reviewing in detail the opinion rendered in this case, the following language is quoted as bearing on the subject under consideration:

> "This great principle is, that the constitution and the laws made in pursuance thereof are supreme; that they control the constitution and laws of the respective States, and cannot be controlled by them. From this, which may be almost termed an axiom, other propositions are deduced as corollaries, on the truth or error of which, and on their application to this case, the cause has been supposed to depend. These are, 1st: that a power to create implies a power to preserve: 2nd: That a power to destroy, if wielded by a different hand, is hostile to, and incompatible with these powers to create and to preserve: 3rd: That where this repugnancy exists, that authority which is supreme must control, not yield to that over which it is supreme. ***** The power of Congress to create, and of course, to continue, the bank, was the subject of the preceding part of this opinion; and is now no longer to be considered as questionable. **** It is of the very essence of supremacy to remove all obstacles

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to its action within its own sphere, and so to modify every power vested in subordinate governments, as to exempt its own operations from their own influence. This effect need not be stated in terms. It is so involved in the declaration of supremacy, so necessarily implied in it, that the expression of it could not make it more certain. We must, therefore, keep it in view, while construing the constitution".

The same question was considered in the case of the Farmers & Mechanics National Bank vs Dearing, reported in 91 U. S. p.33-35, where the constitutional right of Congress to create national banks was discussed. The Court in that case says -

"The constitutionality of the Act of 1864 is not questioned. It rests on the same principle as the Act creating the Second Bank of the United States. The reasoning of Secretary Hamilton and of this court in McCulloch vs Maryland (4 Wheat.316) and in Osborne vs The Bank of the United States (9 id. 708) therefore applies. The national banks organized under the Act are instruments designed to be used to aid the government in the administration of an important branch of the public service. They are means appropriate to that end. Of the degree of the necessity which existed for creating them Congress is the sole judge."

"Being such means, brought into existence for this purpose, and intended to be so employed, the States can exercise no control over them, nor in any wise affect their operation, except in so far as Congress may see proper to permit. Anything beyond this is 'an abuse, because it is the usurpation of power which a single State cannot give'. Against the national will 'the States have no power, by taxation or otherwise, to retard, impede, burthen, or in any manner control, the operation of the constitutional laws enacted by Congress to carry into execution the powers vested in the General Government'. Bank of the United States vs McCulloch, supra; Weston and Others vs Charleston, 2 Pet. 466; Brown vs Maryland, 12 Wheat. 419; Dubbins vs Erie County, id. 419."

"The power to create carries with it the power to preserve. The latter is a corollary from the former".

"The principle announced in the authorities cited is indispensable to the efficiency, the independence, and indeed to the beneficial existence, of the General Government; otherwise it would be liable, in the discharge of its most important trusts, to be annoyed and thwarted by the will or caprice of every State in the

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Union. Infinite confusion would follow. The government would be reduced to a pitiable condition of weakness. The form might remain but the vital essence would have departed."

While this decision relates to national banks, the reasoning will apply with even greater force to Federal reserve banks as agents of the United States Government. This decision has been followed in the case of Haseltine vs Central Bank of Springfield (183 U. S. 135) and Schuyler National Bank vs Gadsden (191 U. S. 457) and in other cases.

It seems to be clear, therefore, that Congress has the right to establish banks with the power to fix interest rates and that these rates are controlled by the Act creating the corporation and not by the State law. In Haseltine vs Central Bank of Springfield, the court says:

"We understand it to be conceded that as the note in question was given to a national bank, the definition of usury and the penalties affixed thereto must be determined by the National Bank Act and not by the law of the State", citing Farmers' and Mechanics National Bank vs Dearing, 91 U. S., 29.

Again, in the case of Schuyler National Bank vs. Gadsden, the Court says:

"This results from the prior adjudications of this court, holding that where usurious interest has been paid to a national bank the remedy afforded by Section 5198 of the Revised Statutes is exclusive and is confined to an independent action to recover such usurious payments".

From these decisions it appears that the interest rates established by State laws apply to loans made by national banks only by reason of the fact that Section 5198 of the Revised Statutes makes such rates applicable, and without the agency of this enactment of Congress the State laws would have no application.

Second. The question of whether or not Congress may delegate to the Federal Reserve Board or to the Federal reserve banks the right to fix interest rates, seems to be clearly established by a number of decisions relating to the right of Congress to delegate to the executive department the right to exercise those powers which are necessary to carry out the purpose of the original Act. For example, in the case of Field vs Clark, 143 U.S. 693, the Court says:

"Legislative power was exercised when Congress declared that the suspension should take effect upon a named contingency. What the President was required to do was simply in execution of the Act of

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"Congress. It was not the making of the law"

Again, in the case of Reagan vs. Farmers Loan and Trust Company, 154 U. S., 393, the Court says:

> "Passing from the question of jurisdiction to the act itself, there can be no doubt of the general power of a state to regulate the fares and freights which may be charged and received by railroad or other carriers, and that this regulation can be carried on by means of a commission. Such a commission is merely an administrative board created by the state for carrying into effect the will of the state as expressed by its legislation. Railroad Commission Cases, 116 U. S. 307".

In Ruttfield vs Stranahan, 192 U. S. 496, the Court says:

> "Congress legislated on the subject as far as was reasonably practicable, and from the necessities of the case was compelled to leave to executive officials the duty of bringing about the result pointed out by the statute. To deny the power of Congress to delegate such a duty would, in effect, amount but to declaring that the plenary power vested in Congress to regulate foreign commerce could not be efficaciously exerted."

In a still later case, the Union Bridge Company vs United States, 204 U. S. 387, the court says:

> "Indeed, it is not too much to say that a denial to Congress of the right, under the Constitution, to delegate the power to determine some fact or the state of things upon which the enforcement of its enactment depends would be 'to stop the wheels of government' and bring about confusion, if not paralysis, in the conduct of the public business."

In view of these decisions there seems to be no question of the right of Congress to delegate the power to fix interest rates with the view of accommodating commerce and business.

Third. In view of the decisions above recited, it seems clear that the failure of Congress to prescribe in the Act itself a maximum rate of interest to be charged will not make the usury laws of the states applicable.

(a) Because, as shown in the cases of the Farmers and Mechanics National Bank vs Dearing, Haseltine vs Central Bank of Springfield, and Schuyler vs Gadsden, supra, the

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state laws have no application in such cases unless the Act of Congress provides that such laws shall be applied.

(b) Because Congress delegated to the Federal reserve banks, subject to review and determination of the Federal Reserve Board, the right to fix rates of discount to be charged by the Federal Reserve banks for each class of paper, such rates to be fixed with the view of accommodating commerce and business.

Respectfully,

Counsel.

Hon. Charles S. Hamlin,
Governor, Federal Reserve Board.

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The following suggestions relating to check clearances are submitted to the Board for its consideration:

While high sounding phrases can be framed about the avoidance of favoritism and the according of uniform treatment to all customers of a bank, there is in reality no such uniformity nor would there be any justice in seeking to apply what might appear to be superficially the same rule to all. Banks do a vast amount of unprofitable business, and nearly all of them carry many accounts as a matter of courtesy and convenience to the depositors which result in actual loss.

Few, if any, practical bankers would concede that there is any injustice in allowing interest on some accounts and refusing it on others, or in furnishing free exchange facilities to some customers and declining to do so in other cases. These matters are usually regulated by mutual agreement and are based upon the general value of an account to the bank, the balance and character of the items received on deposit being taken into consideration. Some dealers prefer to receive interest on their current balances and are willing to pay exchange; others do not care to receive interest but prefer to have their exchanges handled without charge. While from the view point of the bank it might feel justified in allowing interest on accounts showing constant and uniform balances, it would not consider paying anything on spasmodic accounts; then again a bank might very well afford to give free exchange facilities to a customer depositing checks in large amounts on New York and other financial centers while it could not afford to do so in the case of a customer who deposits only checks on small towns.

It is not believed that a Federal reserve bank could legally charge to a bankIs reserve account, over its protest, checks drawn upon the member bank which it had never seen or heard of, nor has a bank, in fact, the right to authorize the payment of a check drawn upon it at a place other than at its own counter, as it might thereby deprive the drawer of his right to stop payment on the check.

It seems, therefore, that the system of clearances authorized by the Act must be developed in an orderly and gradual manner and through the cooperation of the member banks. The problems involved in the clearance of intra-district checks are not very different from those which must be solved in inter-district clearings.

No check coming from either within or outside of a district should be charged to the account of a member bank except by its consent, and no Federal reserve bank should credit a member bank at par on receipt with any check imposing upon it the burden of the time in transit. It is clear that a Federal reserve bank can credit at par on receipt checks drawn on member banks in its Federal reserve city and that common business rivalry will, no doubt, induce member banks in other cities of a reserve district to arrange with the Federal reserve bank, by carrying a deposit in excess of the reserve deposit required, to charge their accounts with checks drawn upon themselves, thereby eliminating the factor of time in transit so far as the Federal reserve bank is concerned. It is not believed, however, that the member banks would care to provide for an immediate debit at the reserve bank of any and all checks that their customers might draw and which might come into the hands of the reserve bank. The Federal Reserve Act expressly recognizes the principle of compensation for a member bank in paying customers' checks that have been sent to a distant city by providing that the Federal Reserve Board may fix a charge that may be imposed by a member bank upon its customers for such service. All banking experience, however, goes to show that such a direct charge, at least at the outset,

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would be so unpopular and would be the subject of as much criticism as to make it impracticable. The member banks, therefore, must find their compensation in the value of the accounts against which the checks are drawn. Possibly all member banks have some customers to whom they are willing to extend unlimited exchange facilities, but it is equally certain that they have other customers to whom they would not think of granting such facilities and who could not reasonably ask such a favor.

The suggestion is made, therefore, that member banks give to customers accorded unlimited exchange facilities a distinctive form of check indicated by a red or blue mark on the upper righthand corner and bearing also a printed or stamped endorsement on the face of the check, as follows:

> "The Federal Reserve Bank of _____ is authorized to charge this check, when remitted by a member bank, or by a Federal reserve bank, or by an officer or agent of the United States, against the account of the (name of bank on which drawn). Such charge will not constitute final payment of this check, which will be forwarded to the (name of bank on which drawn) for actual payment."

A Federal reserve bank should receive on deposit at par for immediate credit from member banks only such checks as are indicated in the manner shown above, and should they do so, would consequently have only such checks to remit to the Federal reserve banks in other districts. The Federal reserve banks should handle ~~unchte~~ unauthorized checks for their member banks as collecting agents only, withholding credit until payment has actually been received.

The Board should suggest to the Federal reserve banks that a regular settling day be agreed upon between them, either once or twice a month, and each Federal reserve bank at the opening of business on each settling day should wire the Federal Reserve Board the figures in even thousands shown on its books to the debit or credit of each other Federal reserve bank. A balance sheet would then be made up in the Secretary's office and each Federal reserve bank would be advised by wire as to the debits and credits necessary to be made in order to offset balances as far as possible. Balances remaining without offset could either run until the next settling day or could be provided for between the banks themselves. It is not the idea that the Board should make any suggestions as to transfers except upon the settling days agreed upon so that every bank may be free to shift balances between settling days to suit itself.

In case the Secretary of the Treasury should be willing to deposit from one to two million dollars with each Federal reserve bank, such deposit being a bookkeeping entry only, the funds to be held here in Washington to the credit of each bank, transfer checks could be drawn by one bank in favor of another against such funds in the Treasury and proper readjustments of balances could be made when necessary.

It should not be forgotten that a check drawn on Tombstone, Arizona, is not and can never be ipso facto worth as much in Boston as a check for the same amount drawn on a bank in Lowell, nor can a check drawn on Augusta, Maine, be worth as much in Portland, Oregon, as it would be in Portland, Maine; therefore the matter of compensation for time in transit should be left to each bank and its individual customer, and an attempt to have the Federal reserve system absorb the float would be not only inequitable, but would stimulate a most unhealthy expansion of credits for the benefit of a portion of the public at the expense of another; it would give impetus to the practice of drawing checks against non-existing balances, and promote enormously the industry of check kiting.

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Regulation No. 155

FEDERAL RESERVE BOARD

Washington, D. C.,

Regulation governing conditions under which National Banks may be granted permission to act as trustee, etc., under Section 11, Subsection K, of the Federal Reserve Act.

I.

Application of national banks to act as trustee, executor, administrator, or registrar of stocks and bonds under Section 11 (K) of the Federal Reserve Act.

1. Any national bank desiring to exercise any or all of the privileges authorized by this section shall make application to the Federal Reserve Board on a form approved by said Board. This application shall be forwarded by the applying bank to the chairman of the board of directors of the Federal reserve bank of the district in which the applying bank is located, and shall thereupon be transmitted to the Federal Reserve Board with the recommendation of the directors of said Federal Reserve bank.

2. There shall be attached to each application the following exhibits:

(a) A statement in detail of the character and extent of the privileges which the applying bank desires to undertake, and if it desires to act as trustee, the statement shall show specifically the nature of such trusteeships and the obligations to be assumed.

(b) A copy of the laws of the State in which such bank is located which relate to the exercise of these powers by corporations.

(c) A copy of the laws relating to the appointment of, and the bonds and reports required of executors and administrators, if the applying bank desires to act in such capacities.

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(d) A copy of the laws, if any, relating to corporations acting as registrars of stocks and bonds, if the applying bank desires to act in such capacity.

II Trust Office.

Each national bank permitted to exercise the powers provided for under this section, shall appoint a trust officer who shall perform his duties under the supervision of a committee to be known as a Trust Committee, to be composed of not less than three members of the board of directors of the bank.

III Provision for keeping Trust Funds.

All funds, securities and investments of every kind held in trust by any national bank granted permission to act as trustee, executor or administrator, shall be segregated and kept separate and apart from any and all other funds, securities and investments of the bank, and separate and apart from one another.

The accounts relating to all such funds, securities and investments, and to all transactions engaged in by the bank as trustee, executor or administrator, shall be so kept that the specific funds, securities or investments belonging to each trust estate may be at all times definitely identified, and such funds shall in no case be carried on the books of the bank as deposits and shall not be so treated in calculating reserve, making loans or in any other manner, but shall at all times be held and treated as trust funds held by the bank in the capacity of trustee, executor or administrator as the case may be.

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IV Investment of Trust Funds.

Trust funds shall be invested in any manner provided in the instrument creating the trust fund or as ordered or authorized by any court of competent jurisdiction or as specifically authorized by the laws of the State in which said national bank is situated. Provided that if there are no contrary instructions as to investments in the instrument creating the trust and no specific provisions of the laws of the State relating thereto, such trust funds, subject to the order of any court of competent jurisdiction may be invested:

(a) In mortgages upon unincumbered and improved real estate situated in the State in which the bank is located, such real estate being of a value, to be ascertained by not less than two disinterested appraisers, equal to double the amount proposed to be invested therein.

(b) In bonds or other interest bearing obligations of the United States or of the District of Columbia.

(c) In the bonds or other interest bearing obligations of any State of the United States, or

(d) In any legally authorized bonds issued by any city, town, county, or other legally constituted municipality or district in the United States which has been in existence for a period of ten years and which for a period of ten years previous to such investment has not defaulted for more than fifteen days in the payment

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of any part of either principal or interest of any funded debt authorized to be contracted by it, and whose not funded indebtedness (as defined in the Regulations of the Board of Trustees of the Postal Savings System approved June 13, 1913) does not exceed ten per cent of the valuation of its taxable property to be ascertained by the last preceding valuation of the property for the assessment of taxes.

Bonds to be eligible under paragraph (c) and (d) above must be the general obligations of the entire State, city, town, county, municipality or district which issues them, it being intended to exclude as ineligible for purchase bonds payable out of the "local benefit" or "special assessment" taxes when the issuing State, city town, county, municipality or district at large is not directly or ultimately liable.

In case of merger, consolidation or succession of any city, town, county, municipality or district the ten year period of existence and non-default referred to in paragraph (d) above will be held to be complied with under the conditions set forth in Section 8-c, paragraphs one, two and three of the regulations of the Board of Trustees of the Postal Savings System for the Guidance of Qualified Banks and Others Concerned as amended November 19, 1914.

V. Trustee under Mortgage or Deed of Trust.

In any case where the bank is named as trustee in any mortgage or deed of trust it shall require a certified copy of the original mortgage or deed of trust to be filed with it and shall at all times keep an accurate account of any bonds outstanding which are secured by such mortgage or deed of trust, and which have been certified to for identification by the trustee. Such records shall be so kept as to enable the bank to furnish the Federal Reserve Board from time to time with any information called for relating to the powers vested in the trustee and the duties imposed by the mortgages or deeds of trust upon such trustee, and to any other matters relating to the exercise of such powers and the

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VI. Statement to Registrar.

L. Before any bank granted permission to act as registrar of stocks and bonds shall countersign any certificate of stock or any bond, or shall register any certificate of stock or any bond, it shall require the corporation issuing this stock or bond to file with it a statement signed by the president or vice-president of the corporation, with the seal of the corporation affixed and attested by the secretary, setting forth fully and accurately the basis or financial plan upon which all stocks and bonds are to be and have been issued.

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Such statement or financial plan shall be in form and shall contain sufficient information in detail to enable the bank acting as registrar to furnish the Federal Reserve Board, or any stockholder or bondholder of the corporation, or any other person entitled thereto, with any information as to the basis of issue of such stock or bonds, the authority for such issue, and the amount outstanding at any time.

VII. Reports.

Whenever the Comptroller of the Currency calls for reports of condition of the bank, such report shall be accompanied by a full statement of the condition of the trust department. Upon request, reports shall also be furnished to the Federal Reserve Board and to the Federal reserve bank of the district in which said bank is located.

VIII. Examination.

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

IX. Security on Bond.

Any national bank acting as trustee, executor, administrator, or registrar of stocks and bonds, shall give such bond as may be required by the laws of the state in which said bank is located, or as may be required by the court appointing it.

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X. Conformity with State Laws.

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

XI. Changes in Rules.

These rules and regulations are subject to changes at any time by the Federal Reserve Board.

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POST OFFICE DEPARTMENT

Third Assistant Postmaster General

WASHINGTON

January 6, 1915.

Hon. C. S. Hamlin,
Governor, Federal Reserve Board,
Washington, D. C.

Sir:

Receipt is acknowledged of the letter of the 30th ultimo from the Secretary of the Federal Reserve Board, inclosing a copy of the report of a committee of your Board with respect to the "definition of duties of the Federal reserve agent," in further reference to your letter of November 24, 1914, inquiring whether Federal reserve agents who are also directors of the Federal reserve banks are entitled to the use of penalty envelopes.

The Federal Reserve Act confers on the Federal Reserve Board the power of appointing three of the directors of the respective Federal reserve banks. These directors are known as "Class C. directors," one of whom is required to be designated by the Federal Reserve Board as chairman of the board of directors of the Federal reserve bank and as Federal reserve agent. The provision of the Act authorizing the appointment of these directors and Federal reserve agents reads as follows:

> "Class C directors shall be appointed by the Federal Reserve Board * * * one of whom shall be designated by said board as chairman of the board of directors of the Federal reserve bank and as 'Federal reserve agent' * * * and in addition to his duties as chairman of the board of directors of the Federal reserve bank he shall

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be required to maintain under regulations to be established by the Federal Reserve Board a local office of said board on the premises of the Federal reserve bank. He shall make regular reports to the Federal Reserve Board, and shall act as its official representative for the performance of the functions conferred upon it by this Act. He shall receive an annual compensation to be fixed by the Federal Reserve Board and paid monthly by the Federal reserve bank to which he is designated."

The law governing the use of penalty envelopes, embodied in section 496, Postal Laws and Regulations, restricts their use to officers of the United States Government. The term "officer of the United States" is defined in the decisions of the Supreme Court in the cases of the United States vs. Mouat, 124 U.S., 303, and United States vs. Smith, 124 U.S., 525. In the former case the Court said:

> "What is necessary to constitute a person an officer of the United States, in any of the various branches of its service, has been very fully considered by this court in United States v. Germaine, 99 U.S., 508. In that case, it was distinctly pointed out that, under the Constitution of the United States, all its officers were appointed by the President, by and with the consent of the Senate, or by a court of law, or the head of a Department; and the heads of the Departments were defined in that opinion to be what are now called the members of the Cabinet. Unless a person in the service of the Government therefore, holds his place by virtue of an appointment by the President, or of one of the courts of justice or heads of Departments authorized by law to make such an appointment, he is not, strictly speaking, an officer of the United States."

In the latter case theCourt said:

> "An officer of the United States can only be appointed by the President, by and with the advice and consent of the Senate, or by a court of law, or the head of a department. A person in the service of the government who does not derive his position from one of these sources is not an officer of the United States in the sense of the Constitution. This

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subject was considered and determined in United States v. Germaine, 99 U.S., 508, and in the recent case of United States v. Mouat, ante, 303. What we have here said is but a repetition of what was there authoritatively declared."

Since the Federal reserve agents are appointed by the Federal Reserve Board and not by the President, or by a court of law, or by the head of a Department, it follows that, under the decisions of the Supreme Court of the United States, they are not "officers of the United States" and, therefore, are not entitled to the use of penalty envelopes.

Furthermore, the Federal Reserve Act provides that the salary of the Federal reserve agent for all his services, both as a director of the bank and as Federal reserve agent, shall be paid by the bank of which he is a director, the Act, in this respect, making a clear-cut distinction between his status and that of the members of the Federal Reserve Board and the "attorneys, experts, assistants, clerks," etc., employed by the Board to conduct its business, whose salaries are paid out of public moneys obtained by assessments on the reserve banks. It also appears that the banks are required to bear the expense of an office maintained for the Federal reserve agent. It, therefore, appears to be the clear intent of the law that each Federal reserve bank shall bear the expenses, including office expenses and postage, incurred by the Federal reserve agent, not only in his capacity as director of the bank, but as such agent as well.

In view of the foregoing, it is held that the Federal reserve agents are not entitled to use penalty envelopes to send in the mails

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free any matters pertaining to their duties as either directors or Federal reserve agents.

Respectfully,

(Signed) A. M. Dockery,

Third Assistant Postmaster General.

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FEDERAL RESERVE BOARD.

Washington

December 30, 1914.

My dear Governor:-

I have your letter of the thirtieth instant, in which you ask for an opinion on the following questions -

> "Whether or not a Federal reserve bank is empowered under the provision of the Federal Reserve Act to act as agent for another Federal reserve bank in the collection of maturing notes, drafts, bills of exchange and other evidences of debt purchased under the provisions of the Act by the Federal reserve bank, which items are payable within the district of the Federal reserve bank to which they are sent".

The exercise of this power would require the collecting bank to act as agent for the forwarding bank in the collection of the items mentioned in your letter since, in such case, under the uniform decisions of the Court, the agency continues until the items are collected. This right is not specifically included in the powers of the Federal reserve banks enumerated in the Federal Reserve Act. Section Thirteen, in dealing with the subject of collections, provides -

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

It will be observed that the language used in the Section above quoted does not specifically include notes, drafts and bills of exchange but Federal reserve banks are authorized to receive <u>deposits</u> of current funds in lawful money, national-bank notes, or checks and drafts upon solvent member or other Federal reserve banks, payable upon presentation. The question therefore arises, whether or not such notes, drafts and bills of exchange may be accepted by Federal reserve banks in the capacity of agent for other

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Federal reserve banks and the determination of this question is dependent upon whether or not this power may be said to be incidental to those powers which are specifically granted. Section Four, sub-section 7, of the Federal Reserve Act, in defining some of the corporate powers of Federal reserve banks, reads as follows:

> "To exercise by its board of directors, or duly authorized officers or agents, all powers specifically granted by the provisions of this Act, and such incidental powers as shall be necessary to carry on the business of banking within the limitations prescribed by this Act".

This language is substantially similar to the language used in Section 5136 of the Revised Statutes which deals with the corporate powers of national banks. Section Seventh of this Section reads as follows:

> "To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this Title".

It will be observed that in defining the powers of national banks, as well as in defining the powers of Federal reserve banks, Congress has not specifically authorized such banks to act as agent for other banks. The powers enumerated, however, in both instances, are what may be termed contractural powers of a Federal reserve bank or a national bank; that is to say, the Act defines and limits under what conditions such banks may become indebted to others or may permit others to become indebted to such banks.

In the matter of collection of items mentioned in your letter, however, the relation of debtor and creditor is not established as between the forwarding bank and the collecting bank until the item sent for collection is actually collected; and where the instructions of the forwarding bank are to collect and remit the bank receiving such items has this single duty to perform and the proceeds are not credited to the forwarding bank after collection but are remitted to such bank. If the instructions accompanying such items are to collect and credit, then the collecting bank collects from the drawee of the draft or the obligor of the note, funds which it may receive on deposit, and, consequently, when its

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agency terminates it exercises a power specifically granted to it, namely, the power to receive deposits. Accordingly, it seems clear that the collection of items referred to by you may be said to be incidental to the power to receive deposits.

Banks very generally act as agents for other banks in making collections of this sort and the right of national banks to perform this duty has, so far as I have been able to learn, never been questioned; on the contrary, there are a number of cases holding that in the matter of collection of items banks, as stated, act only as agents until the item has been actually collected.

This is true even in the case of deposit of checks by individuals with national banks.

The Courts have held that even though credit may be given in the pass book for the check upon its deposit, the bank continues as the agent of the depositor until the check has been collected.

It seems to me, therefore, that unless as a matter of policy the Board determines that the Federal reserve banks are not ready to act as collecting agents for other Federal reserve banks in the collection of the items enumerated by you, there is no reason why this power should not be exercised without exceeding the corporate powers granted by statute, and those incidental to the specific powers granted.

Respectfully,

(Signed) M. C. Elliott

Counsel.

Hon. Charles S. Hamlin,
Governor.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

January 5th, 1915.

My dear Governor:-

I have your letter of the fourth instant asking for an interpretation by this office of that part of Section Sixteen of the Federal Reserve Act which reads as follows:

> "Any Federal reserve bank may at any time reduce its liability for outstanding Federal reserve notes by depositing, with the Federal reserve agent, its Federal reserve notes, gold, gold certificates, or lawful money of the United States. Federal reserve notes so deposited shall not be reissued, except upon compliance with the conditions of an original issue.
>
> The Federal reserve agent shall hold such gold, gold certificates, or lawful money available exclusively for exchange for the outstanding Federal reserve notes when offered by the reserve bank of which he is a director. Upon the request of the Secretary of the Treasury the Federal Reserve Board shall require the Federal reserve agent to transmit so much of said gold to the Treasury of the United States as may be required for the exclusive purpose of the redemption of such notes".

The question for determination, as I understand it, is whether or not Federal reserve banks may deposit lawful money for the retirement of Federal reserve notes issued to such bank when the notes to be retired are still in the possession of the bank making the deposit. This question involves a construction of the language "outstanding Federal reserve notes". Does this mean notes which have left the possession of the Federal reserve agent, or does it have reference to notes which have been placed in actual circulation by the Federal reserve bank and have left the possession of such bank?

In a purely technical sense Federal reserve notes which are obligations of the United States Government become outstanding obligations when the Federal reserve agent delivers them to the bank applying therefor, and where this language is used in other parts of the Act it should probably be given this construction. In the present instance,

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however, the Federal reserve bank obtaining such notes is one of the places of redemption. Accordingly, the term "outstanding" appears to be used in the statute in a dual sense. That is to say, it refers to those notes which are outstanding obligations of the United States when they have left the possession of the Federal reserve agent, and also to those notes which become outstanding liabilities of a Federal reserve bank when they have left the possession of the Federal reserve bank. This is indicated by that part of the Act which in referring to such notes, reads

> "They shall be redeemed in gold on demand at the Treasury Department of the United States, or in gold or lawful money at any Federal reserve bank".

In order for such notes to be offered for redemption at any Federal reserve bank, it is necessary for them to be in actual circulation and not in possession of such Federal reserve bank. It is necessary, in construing this language, to consider this distinction.

It will be observed, as stated, that these notes are redeemed by presentation to the Treasurer at Washington, or by presentation to the Federal reserve bank, and the Federal reserve bank in turn presents them to the Federal reserve agent for exchange for lawful money deposited by the Federal reserve bank.

This being true, it was evidently contemplated by Congress that any Federal reserve bank desiring to reduce its liability for Federal reserve notes which are outstanding obligations of the United States, that is to say - Federal reserve notes which have left the possession of the Federal reserve agent, may deposit with the Federal reserve agent any Federal reserve notes in its possession. Having done this, if it desires to further reduce its liability for outstanding Federal reserve notes, that is to say - Federal reserve notes which have left the possession of the Federal reserve bank, it may do so by depositing gold or lawful money with the Federal reserve agent.

In this latter case, whenever Federal reserve notes are presented to the Federal reserve bank for redemption, after it has deposited lawful money with the Federal reserve agent to reduce its liability, the Federal reserve bank receiving such notes should immediately present them for redemption to the Federal reserve agent and receive in exchange therefor the lawful money so deposited.

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The Federal reserve agent is required, as above stated, to hold the lawful money deposited available exclusively for the redemption of such Federal reserve notes when presented by the Federal reserve bank and in order for him to use the funds so deposited for the purpose for which they are deposited, it is a condition precedent that the Federal reserve bank should present notes coming into its possession for exchange. The Federal reserve bank in such case, having discharged its liability, should not be permitted to put back into circulation any such notes coming into its possession but should be required to present them for redemption as the statute clearly contemplates.

It will be recalled that banks are expected to pay the rate of interest on such notes fixed by the Federal Reserve Board, and it is to be assumed that no bank having in its possession Federal reserve notes and lawful money would deposit the lawful money with the Federal reserve agent and continue to pay interest charged on the Federal reserve notes.

A regulation requiring the presentation of such notes to the Federal reserve agent when they come into the possession of the Federal reserve bank under such circumstances would, therefore, seem to be entirely in accord with the purposes and intent of this Act.

Respectfully,

(Signed) M. C. Elliott

Counsel.

Hon. Charles S. Hamlin,
Governor, Federal Reserve Board.

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F E D E R A L R E S E R V E B O A R D

Washington.

January 4, 1915.

My dear Governor:

By direction of the Board, the Secretary has referred to this office for an opinion that portion of the report of the Advisory Council submitted by Mr. J. B. Forgan, President, which deals with the subject of check clearings. The part of the report referred to reads as follows:

> "Check Clearings.
>
> The Federal Advisory Council is unable at present to make definite suggestions on this subject.
>
> As a preliminary the Federal Reserve Board or its counsel should determine whether under Sections 13 and 16 of the Federal Reserve Act, Federal reserve banks are either permitted or required to receive on deposit from their depositors checks drawn upon member banks or Federal reserve banks of other districts. As the Council reads these sections such checks can only be received on deposit by a Federal reserve bank "when remitted by" another Federal reserve bank and then solely for exchange purposes. In the opinion of the Council it is unsound in principle and wrong in practice that a check drawn on a member bank should be charged to its reserve account with a Federal reserve bank without its authority and without its having had an opportunity to pass upon it. The Council fears that the attempt being made by some of the Federal reserve banks to disregard the elements of time and distance in connection with the clearing of bank checks may so involve and absorb the funds of the Federal reserve banks as to seriously impair their usefulness as banks of issue and discount."

It will be observed that two questions are presented for consideration -

First, Can a Federal reserve bank, under the terms of the Act, be permitted or required to accept on deposit checks and drafts drawn against banks which are members of other Federal reserve banks.

Second, Can a Federal reserve bank, receiving on deposit or by remittance from another Federal reserve bank checks or drafts drawn against one of its member banks,

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charge up such checks or drafts against the reserve or deposit account of a member bank without instructions or authority from such member bank.

While these two questions may be said to be related, or at least that both are to be considered as part of the general subject of clearances, the legal questions involved are distinct and they should be considered separately.

The first question involves an interpretation of the language of Sections 13 and 16, to which Mr. Forgan calls attention, and which relates to specific powers of Federal reserve banks, and also to an interpretation of Section 4, Sub-section 7th, of the Federal Reserve Act which deals with the general corporate powers of Federal reserve banks. That part of Section 13 which relates to this subject reads as follows:

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

That part of Section 16 which relates to this subject matter reads as follows:

> "Every Federal reserve bank shall receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors, and when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank or member bank upon funds to the credit of said depositor in said reserve bank or member bank. Nothing herein contained shall be construed as prohibiting a member bank from charging its actual expense incurred in collecting and remitting funds, or for exchange sold to its patrons. The Federal Reserve Board shall, by rule, fix the charges to be collected by the member banks from its patrons whose checks are cleared through the Federal reserve bank and the charge which may be imposed for the service of clearing or collection rendered by the Federal reserve bank.
>
> The Federal Reserve Board shall make and promulgate from time to time regulations governing the transfer of funds and charges therefor among Federal reserve banks and their branches, and may at its discretion

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exercise the functions of a clearing house for such Federal reserve banks, or may designate a Federal reserve bank to exercise such functions, and may also require each such bank to exercise the functions of a clearing house for its member banks."

Section 4, Sub-section 7th, in dealing with the general corporate powers of banks reads as follows:

"To exercise by its board of directors, or duly authorized officers or agents, all powers specifically granted by the provisions of this Act and such incidental powers as shall be necessary to carry on the business of banking within the limitations prescribed by this Act."

In passing upon the questions under consideration it is necessary to consider together the foregoing provisions of the Federal Reserve Act in determining (a) whether the power to receive such items on deposit is a power specifically granted by the Act, or (b) if not specifically granted, is the exercise of this power necessarily incident to any power which is specifically granted.

It needs no citation of authority to sustain the proposition that although not specifically granted, a power may be exercised which is necessarily incident to a power which is granted. This is not only the well recognized American rule relating to corporate powers but such rule is specifically recognized by Section 4, Sub-section 7th, above quoted.

Considering the question from the first standpoint, Section 13 provides that "any Federal reserve bank may receive from any of its member banks deposits of .... checks and drafts upon solvent member banks . . . . or, solely for exchange purposes, may receive from other Federal reserve banks deposits of . . . . checks and drafts upon solvent member or other Federal reserve banks. . . . ."

Section 16 provides that "Every Federal reserve bank shall receive on deposit . . . . when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank or member bank upon funds to the credit of said depositor in said reserve bank or member bank."

It will be observed from the foregoing that under Section 13 Federal reserve banks may receive from their own members checks and drafts upon solvent member banks. It is necessary, therefore, to determine the meaning of the language checks and drafts upon solvent member banks. Does this mean banks which are members of the same Federal reserve

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bank as the depositing bank, or may a bank deposit in the Federal reserve bank of which it is a member checks or drafts drawn against banks which are solvent member banks of other Federal reserve banks?

The term "member bank" is defined by Section 1 as "any national bank, State bank, or bank or trust company which has become a member of one of the reserve banks created by this Act".

Attention is called to the fact that the bank which is authorized to make the deposit in a Federal reserve bank is designated as "any of its member banks" while in designating the bank against which items may be drawn this prosessive pronoun is omitted and the language used is "checks and drafts upon solvent member banks". The omission of this qualification is doubly significant in the next clause where the statute provides that "solely for exchange purposes may receive from other Federal reserve banks.....checks and drafts upon solvent member or other Federal reserve banks".

In this latter case the statute not only fails to qualify which member banks such checks and drafts must be drawn against to be received but the context clearly shows that Federal reserve banks are expected to receive checks and drafts on banks which are members of other Federal reserve banks. For example, let us assume that the checks sent to the Federal reserve bank solely for exchange purposes by another Federal reserve bank are checks and drafts drawn against the receiving bank. It necessarily follows that the forwarding Federal reserve bank must have previously received such items from some source, that is to say, from one of its member banks, from the United States Government or from some other Federal reserve bank.

It would seem clear, therefore, that the language "checks and drafts upon solvent member banks" must be construed to mean checks and drafts drawn against banks which are members of any Federal reserve bank.

The same conclusion seems inevitable in Section 16 since a Federal reserve bank could not remit items drawn against depositors of other Federal reserve banks without first receiving such items from some source. If there should be any doubt as to this interpretation of the language "solvent member banks" and the conclusion should be reached that the power to receive checks and drafts on banks which are members of other Federal reserve banks is not specifically granted by statute, such a power must nevertheless be construed as a power incidental to those powers which are specifically granted for the reasons above stated.

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The second question raised in the report referred to relates, as stated, to the right of a Federal Reserve bank to charge items sent it for collection against the account of a member bank without authority from such member bank. Mr. Forgan states that

> "In the opinion of the Council it is unsound in principle and wrong in practice that a check drawn on a member bank should be charged to its reserve account with a Federal reserve bank without its authority and without its having had an opportunity to pass upon it".

I am not entirely clear upon just what theory a Federal reserve bank undertakes to charge up items drawn against other banks without authority from such bank. When a member bank makes a deposit in a Federal reserve bank to its reserve account, or to any other account, the relation of debtor and creditor is immediately established as between the Federal reserve bank and such member bank, and the credit balance thus created can legally be drawn against only by the depositing bank.

When any bank receives on deposit checks or drafts drawn against other banks, such items are accepted for collection as agent for the depositor and this agency continues until the items are actually collected.

It is true that in many instances the bank receiving such items on deposit immediately credits these items to the account of the depositor but where this is done it is credit extended upon the responsibility of the depositor and the bank reserves the right to charge back such items to the depositor's account if they are returned unpaid. Where the items are forwarded to correspondent banks for collection such banks in turn accept them as agents and the relation of debtor and creditor is not finally established until the check or draft is actually paid by the bank against which it is drawn. The decisions of our courts are uniform on this subject. Accordingly, where a Federal reserve bank in due course of business receives checks or drafts from any source for deposit or collection it acts merely as the agent for the depositor until such items are collected, and as such agent it has no right to appropriate funds held by it belonging to the bank against which such items are drawn for the payment of such items without specific authority from the bank in question. The depositing bank and not the bank against which such items are drawn is liable to the Federal reserve bank for any credit given to such depositing bank on the strength of such items, and the question of whether or not the depositing bank should be given credit immediately, or after the items are collected, is one for consideration by the Board.

Respectfully,
(Signed) H. C. ELLIOTT
Counsel

Hon. Charles S. Hamlin,
Governor.

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FEDERAL RESERVE BOARD

WASHINGTON

January 4, 1915.

MEMORANDUM FOR GOVERNOR HAMLIN.

My dear Governor:

I have your letter of January 2nd and have carefully examined that part of Section 18 of the Federal Reserve Act which relates to the exchange of United States bonds with the circulating privilege for one year gold notes of the United States and thirty year 3% gold bonds without the circulating privilege.

After analysing this whole section and after considering all the circumstances, I am inclined to the view that technically the Federal Reserve Board has the right at this time to authorize this exchange and that the opening sentence of this section making certain provisions effective only after two years from the passage of the Act, does not relate to the provision under consideration.

As heretofore advised the power to purchase bonds having the circulation privilege and to issue national currency against such bonds is specifically given to the Federal reserve banks by other sections of the Act.

When Section 18 was incorporated in the Act it was originally intended, as its title implies, to provide a method for gradually refunding bonds held at the time by the several national banks. This matter was very carefully considered by the Committee of the House and the Committee of the Senate and a number of plans were submitted having for their object the ultimate retirement of national bank circulation and the substitution of other notes. At the time of the passage of the Act there was approximately $750,000,000. in national bank circulation outstanding. The bonds securing this circulation mature at the pleasure of the United States Government after thirty years from the date of issue and it was accordingly estimated that if the Federal reserve banks could acquire a minimum of $25,000,000. a year they would have in their possession at the maturity of these bonds approximately the entire issue, and the Government would have to deal

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only with the Federal reserve banks instead of with the several thousand national banks in refunding such bonds.

It was recognized, however, that unless the national banks desired to retire their circulation the Federal reserve banks would be unable to procure the bonds, and this method was provided of having those national banks desiring to retire the whole or any part of their circulation make application through the Treasurer to sell the bonds for their account and the Federal Reserve Board was empowered to require Federal reserve banks to purchase bonds so offered, and, as suggested by you, it was originally contemplated that the Federal reserve banks should thereupon be required to issue Federal reserve bank notes against such bonds.

In view of the arguments presented to the Committee that this circulation becomes redundant at certain times, it was later determined to permit the exchange of bonds thus acquired with the circulating privilege for obligation of the United States without the circulating privilege.

As stated, this section was originally intended to deal only with the bonds acquired from national banks desiring to retire in whole or in part their national bank circulation.

The section was amended, however, in conference so that is now provides -

(a) for the issuance of Federal reserve bank notes against bonds acquired under other provisions of the Act as well as against bonds acquired under this section; and

(b) for the exchange of any United States 2% gold bonds bearing the circulation privilege but against which no circulation is outstanding for one year gold notes of the United States without the circulation privilege to an amount not to exceed one-half of the 2% bonds so tendered for exchange and the thirty year 3% gold bonds, without the circulating privilege, for the remainder of the bonds so tendered.

It is significant that in the first two paragraphs of this section in referring to the bonds which the

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Federal reserve banks may be required to purchase, Congress uses the words "such bonds" manifestly referring to bonds which a national bank desires to sell through the Treasurer in order to reduce its circulation.

In the fifth paragraph of this section, however, it is provided:-

> "Upon the deposit with the Treasurer of the United States of bonds so purchased or any bonds with the circulating privilege acquired under Section four of this Act, any Federal reserve bank*** shall be entitled to receive *** circulating notes *** equal in amount to the par value of the bonds so deposited."

In this paragraph the section for the first time refers to bonds other than those acquired from banks desiring toreduce their circulation and in the following paragraph the language of the Act is -

> "Upon application of any Federal reserve bank approved by the Federal Reserve Board, the Secretary of the Treasury may issue in exchange for United States 2% gold bonds bearing the circulation privilege, but against which no circulation is outstanding one-year gold notes," etc. etc.

The failure therefore to restrict this paragraph by any qualifying clause the bonds which may be exchanged other than the qualification that they shall be 2% United States bonds with the circulating privilege, would seem to indicate that the Federal Reserve Board may, in its discretion, authorize the exchange of any bonds bearing this privilege acquired in any manner by the Federal reserve banks.

In this connection, however, attention is called to the fact that this exchange involves the exercise of a discretion on the part of the Federal Reserve Board and there would seem to be a strong reason, as a matter of policy, for the Board to refuse to exercise this discretion until the expiration of the two years or at least until a later date.

The two year limitation was imposed in order that the Federal reserve banks might have an opportunity to become firmly established before they shall be required

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to take over bonds from national banks and there would seem to be a still stronger reason for waiting until this time before permitting them to exchange bonds so acquired for one year gold notes. Such an exchange would require the Federal reserve bank receiving such one year gold notes to enter into an obligation to purchase new notes when those issued mature and were paid and it is only upon this condition that the Government can undertake under the Act to exchange these short term obligations for the thirty year 3% bonds. Accordingly the Federal reserve bank should not be permitted to assume this obligation until it has become firmly established.

I would respectfully suggest, therefore, that Mr. Perrin be advised that the Board cannot at this time approve the exchange suggested and that the matter be left open of whether or not the Board can legally authorize such an exchange before the expiration of two years.

Respectfully,

(Signed) M. C. Elliott

Counsel.

Honorable Charles S. Hamlin,
Governor, The Federal Reserve Board.

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Form 26-a. 181.

FEDERAL RESERVE BOARD
Washington

181

Notice of call for payment of first installment of subscription to capital stock of and the transfer of reserves to the Federal Reserve Bank of_____

To the _____Bank,

_____

In accordance with the provisions of Sections 2 and 5 of the Act approved December 23, 1913, and known as the Federal Reserve Act, the Federal Reserve Board has fixed_____, as the date of payment of the first installment of your subscription to the capital stock of the Federal Reserve Bank of your district.

You are accordingly hereby notified that remittance should be made to the Federal Reserve Bank of _____, of a sum in gold equal to one-sixth of the total amount of capital stock allotted to you, such remittance to be made on or before the date above specified.

Under the terms of Section 2 of the Federal Reserve Act, the second installment of one-sixth of your subscription must be paid within three months from date of this call,_____, and the third installment of one-sixth of your subscription must be paid within six months from said date. The remainder of your subscription, or any part thereof, shall be subject to call when deemed necessary by the Federal Reserve Board.

Remittance must be made in gold or gold certificates. If checks or drafts on other banks are used, arrangements should first be made with the bank on which such drafts are drawn to make payment in gold or gold certificates, and the Federal Reserve Bank to which such checks or drafts are sent can receive same only for collection.

You are also hereby notified that on the said date you should transfer to the Federal Reserve Bank of your district the installment of your reserves required by Section 19 of the Federal Reserve Act. Remittance should be made in the manner provided by law.

THE FEDERAL RESERVE BOARD,
By Charles S. Hamlin, Governor.

H. Parker Willis, Secretary.

RECEIPT FOR NOTICE OF CALL

(This receipt should be filled out, detached and returned promptly in the enclosed envelope, which requires no postage.)

Receipt is hereby acknowledged of notice of call by the Federal Reserve Board for payment of the first installment of this bank's subscription to the capital stock of and the transfer of reserves to the Federal Reserve Bank of _____

_____

By_____Cashier.

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Tentative Regulation.

FEDERAL RESERVE BOARD

Washington, D. C.

Regulations governing conditions under which National Banks may be granted permission to act as trustee, etc., under Section 11, Subsection K, of the Federal Reserve Act.

I.

Application of member banks to act as trustee, executor, administrator, transfer agent, or registrar of stocks and bonds under Section 11 (K) of the Federal Reserve Act.

1. Any member bank desiring to exercise any or all of the privileges authorized by this section shall make application to the Federal Reserve Board on a form approved by said Board. This application shall be forwarded by the applying bank to the chairman of the board of directors of the Federal reserve bank of its district, and shall thereupon be transmitted to the Federal Reserve Board with the recommendation of the directors of said Federal reserve bank.

2. There shall be attached to each application the following exhibits,

(a) A statement in detail of the character and extent of the privileges which the applying bank desires to undertake, and if it desires to act as trustee, the statement shall show specifically the nature of such trusteeships and the obligations to be assumed.

(b) A copy of the laws of the state in which such bank is located, which relate to the exercise of these powers by corporations.

(c) A copy of the laws relating to the appointment of, and the bonds and reports required of executors and administrators, if the applying bank desires to act in such capacities.

(d) A copy of the laws, if any, relating to corporations acting as transfer agents and registrars of stocks and bonds, if the applying bank desires to exercise this privilege,

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II. Separate Departments.

Each National bank permitted to act under this section, shall establish a separate trust department and place it under the management of a trust officer who shall perform his duties under the supervision of a committee to be known as a Trust Committee, composed of not less than three members of the board of directors of the bank.

III. Provision for keeping Trust Funds.

The funds, securities and investments held in trust shall be held separate and distinct from the general funds and securities of the bank, and separate and distinct from each other. A separate vault, safe or compartment shall be provided by each bank acting under this section, in which the funds and securities belonging to its trust department shall be kept, and the ledgers and other books kept for the trust department shall be entirely separate and apart from the other books and records of the bank. The trust officer shall not be permitted to deposit any funds of the trust department with his own bank, but may be permitted by resolution of the board of directors to open such accounts as may be necessary in the name of the trust department in some other bank or banks.

IV. Investment of Trust Funds.

Trust funds may be invested in any manner provided in the instrument creating the trust fund or as ordered or authorized by any court of competent jurisdiction or as specifically authorized by the laws of the state in which said National bank is situated.

V. Trustee under Mortgage or Deed of Trust.

In any case where the bank is named as trustee in any mortgage or deed of trust it shall require a certified copy of the original mortgage or deed of trust to be filed with it and shall at all times keep an accu-

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rate account of any bonds outstanding which are secured by such mortgage or deed of trust, and which have been certified to for identification by the trustee. Such records shall be so kept as to enable the bank to furnish the Federal Reserve Board or the Federal Reserve Bank from time to time with any information called for relating to the powers vested in the trustee and the duties imposed by the mortgage or deeds of trust upon such trustee, and to any other matters relating to the exercise of such powers and the performance of such duties.

VI. Transfer Agent and Registrar.

Any bank granted permission to act as Transfer Agent or Registrar of stocks and bonds shall have the privilege of acting in either capacity, but shall not act in both capacities with respect to the same issue of stocks or bonds. Before acting in either capacity the bank shall require the corporation issuing the stock or bond to file with it a statement signed by the president or vice president of the corporation, with the seal of the corporation affixed, and attested by the secretary, setting forth fully and accurately the basis or financial plan upon which all stocks and bonds are to be and have been issued, also a list giving the number of all stocks or bonds outstanding with the names of registered holders and dates of issue.

Such statement or financial plan shall be in form and shall contain sufficient information in detail to enable the bank acting as transfer agent or registrar to furnish the Federal Reserve Board, or any stockholder or bondholder of the corporation, or any other person entitled thereto, with any information as to the basis of issue of such stock or bonds, the authority for such issue, and the amount outstanding at any time.

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VII. Reports.

Whenever the Comptroller of the Currency calls for reports of condition of the bank, such report shall be accompanied by a full statement of the condition of the trust department. Upon request, reports of the trust department shall also be furnished to the Federal Reserve Board and to the Federal reserve bank of the district in which said bank is located.

VIII. Examination.

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

IX. Security on Bond.

Any National bank acting as trustee, executor, administrator, transfer agent or registrar of stocks and bonds, shall give such bond as may be required by the laws of the state in which said bank is located, or as may be required by the court appointing it.

X. Conformity with State Laws.

Nothing in these regulations shall be construed to give to a national bank doing business as trustee, executor, administrator, transfer agent, or registrar of stocks and bonds under Section 11 (K) of the Federal Reserve Act, any rights or privileges in contravention of the laws of the state in which the bank is located.

XI. Changes in Rules.

These rules and regulations are subject to change at any time by the Federal Reserve Board.

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Regulation No. _____

FEDERAL RESERVE BOARD.

Washington, D. C. _____

Regulations governing conditions under which National banks may be granted permission to act as trustee, etc., under Section 11, Subsection K of the Federal Reserve Act.

I.

Application of national banks to act as trustee, executor, administrator, or registrar of stocks and bonds under Section 11 (K) of the Federal Reserve Act.

1. Any National bank desiring to exercise any or all of the privileges authorized by this section shall make application to the Federal Reserve Board on a form approved by said Board. This application shall be forwarded by the applying bank to the chairman of the board of directors of the Federal reserve bank of its district, and shall thereupon be transmitted to the Federal Reserve Board with the recommendation of the directors of said Federal reserve bank.

2. There shall be attached to each application the following exhibits:

(a) A statement in detail of the charactor and extent of the privileges which the applying bank desires to exercise, and if it desires to act as trustee, the statement shall show specifically the nature of the trusteeships and the character of the obligations to be assumed.

(b) A copy of the laws of the state in which such bank is located, which relate to the exercise of trustee powers by corporations, if the applying bank desires to act in such capacity.

(c) A copy of the laws relating to the appointment of, and the bonds and reports required of, executors and administrators, if the applying bank desires to act in such capacities.

(d) A copy of the laws, if any, relating to corporations acting as transfer agents and registrars of stocks and bonds, if the applying bank desires to exercise this privilege.

II. Separate Departments.

Each National bank permitted to act under this section, shall establish a separate trust department and place it under the management of a trust officer or officers whose duties shall be performed under the supervision of a committee to be

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known as a Trust Committee, composed of not less than three members of the board of directors of the bank.

III. Provision for keeping trust funds.

The funds, securities and investments held in trust shall be held separate and distinct from the general funds and securities of the bank, and separate and distinct from each other. A separate vault, safe or compartment shall be provided by each bank acting under this section, in which the funds and securities belonging to its trust department shall be kept, and the ledgers and other books kept for the trust department shall be entirely separate and apart from the other books and records of the bank. The trust officer shall not be permitted to deposit any funds of the trust department with his own bank, but may be permitted by resolution of the board of directors to open such accounts as may be desirable in the name of the trust department in some other bank or banks. The bank however, shall be responsible for any funds so deposited.

IV. Investment of funds.

Trust funds may be invested in any manner provided in the instrument creating the trust fund, or as ordered or authorized by any court of competent jurisdiction, or as corporations or individuals acting as trustee are specifically authorized by the laws of the state in which said National bank is situated. In case there are no specific provisions in the laws of the state relating to the investment of trust funds, the Federal Reserve Board will deal with this question in passing upon applications of banks located in such states.

V. Trustees under Mortage or Deed of Trust.

In any case where the bank is named as trustee in any mortgage or deed of trust it shall require the original mortgage or deed of trust, showing proper certificate of record, to be filed with it and shall at all times keep an accurate account of all bonds outstanding which are secured by such mortage or deed of trust, or which have been certified to for identification by the trustee,

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and also shall keep a record of all such bonds which have been converted or cancelled.

VI. Registrar of Stocks and Bonds.

Before any bank granted permission to act as registrar of stocks and bonds shall countersign any certificate of stock or any bond, or shall register any certificate of stock or any bond, it shall require the corporation issuing this stock or bond to file with it a statement signed by the president or vice president of the corporation with the seal of the corporation affixed, and attested by the secretary, setting forth the total authorized and the total outstanding stocks and bonds of the corporation, and the par value of each, specifying the number of common and the number of preferred shares, also, where the bank is to be registrar of a stock issue, a list showing the names of the owners and the number of shares of outstanding stock held by each, and, where bonds are to be registered, a list containing the names of the holders of such registered bonds.

Any bank acting as registrar shall maintain records showing in detail all stocks or bonds registered and cancelled.

VII. Reports.

Whenever the Comptroller of the Currency calls for reports of condition of the bank, such report shall be accompanied by a full statement of the condition of the trust department. Upon request, reports of the trust department shall also be furnished to the Federal Reserve Board and to the Federal reserve bank of the district in which said bank is located.

VIII. Examination.

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

IX. Security on Bond.

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of stocks and bonds, shall give such bond as may be required by the laws of the state in which said bank is located, or as may be required by the court appointing it.

X. Conformity with State Laws.

Nothing in these regulations shall be construed to give to a National bank doing business as trustee, executor, administrator, or registrar of stocks and bonds under Section 11(K) of the Federal Reserve Act, any rights or privileges in contravention of the laws of the state in which the bank is located.

Xl. Changes in Rules.

These rules and regulations are subject to change at any time by the Federal Reserve Board.

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FEDERAL RESERVE BOARD 190

January 18, 1915.

SUBJECT: Exchange Charges.

My dear Governor:-

As requested, I have examined the provisions of Section Sixteen of the Federal Reserve Act which relate to the subject of exchange charges with the view of determining to what extent member banks and Federal reserve banks are limited by the terms of the Act in charging for collection of items received on deposit.

The provisions of the Act relating to this subject are not entirely consistent and free from ambiguity and following the usual rule of construction in such cases it is necessary to consider the several provisions as a whole in order to reach a conclusion as to the intention of Congress.

Section 16 provides in part as follows -

> "Every Federal reserve bank shall receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors, and when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank or member bank upon funds to the credit of said depositor in said reserve or member bank. Nothing herein contained shall be construed as prohibiting a member bank from charging its actual expense incurred in collecting and remitting funds, or for exchange sold to its patrons. The Federal Reserve Board shall, by rule, fix the charges to be collected by the member banks from its patrons whose checks are cleared through the Federal reserve bank and the charge which may be imposed for the service of clearing or collection rendered by the Federal reserve bank."

It will be observed from the foregoing that every Federal reserve bank is required (a) to receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors, and (b) when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank

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or member bank upon funds to the credit of said depositor in said reserve bank or member bank.

Without the further provisions of the Act it would seem clear that Congress intended to require Federal reserve banks to collect all checks and drafts without any charge to the depositing bank. The concluding sentence of this paragraph, however, negatives this idea since it states in terms that "The Federal Reserve Board shall, by rule, fix the charges to be collected by the member bank from its patrons whose checks are cleared through the Federal reserve bank and the charge which may be imposed for the service of clearing or collection rendered by the Federal reserve bank."

The question, therefore, arises if both the member banks and Federal reserve banks are to be permitted to make some charge for the service of collection, what meaning is to be given to the words used in the first part of the paragraph "AT PAR". Ordinarily, the language to "receive on deposit at par" could only be interpreted to mean at the face value of such checks or drafts and if credit is given depositors at the face value, manifestly no deduction can be made for the service of collection.

From an examination of the bill as it passed the House and the Senate, and as it was agreed to by the Conference Committee, it appears that according to the House bill no charges of any kind were to be allowed the Federal reserve banks for making collections. The exact language used was as follows -

> "It shall be the duty of every Federal reserve bank to receive on deposit at par, and without charge for exchange or collection, checks and drafts drawn upon any of its depositors or by any of its depositors upon any other depositor, and checks and drafts drawn by any depositor in any other Federal reserve bank upon funds to the credit of said depositor in said reserve bank last mentioned."

When the bill passed the Senate, however, it was amended to read as follows:

> "Every Federal reserve bank shall receive on deposit from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors, and when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank or member bank upon funds to the credit of said depositor in said reserve bank or member bank.... .....The Federal Reserve Board may, by rule, fix the charges to be collected by the member banks from its

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> patrons whose checks are cleared through the Federal reserve bank and the charge which may be imposed for the service of clearing or collection rendered by the Federal reserve bank."

From this it appears that the Senate intended to eliminate the provision of the House bill requiring this service to be rendered without charge and to leave the amount of such charges to the discretion of the Federal Reserve Board.

When the bill was submitted to the Conference Committee, this Committee adopted the language quoted in the Senate bill but restored the words "AT PAR" and changed the provision giving the Federal Reserve Board power in its discretion to fix by rule the charges to be collected so as to make it mandatory on the Board to do so rather than to leave it a matter of discretion, - that is to say, it substituted the words "SHALL" for the word "MAY", and so the Act as it finally passed reads -

> "The Federal Reserve Board shall, by rule, fix the charges to be collected by the member banks from its patrons whose checks are cleared through the Federal reserve bank and the charge which may be imposed for the service of clearing or collection rendered by the Federal reserve bank."

As suggested, there is an apparent inconsistency in these provisions in that the checks and drafts are to be received at par and yet the Federal Reserve Board is required to fix a charge for the services rendered in collecting such items. This being true, it is necessary to consider the express provision that charges are to be made as a qualification of the language that checks and drafts are to be received at par, and reading these two provisions together, it would seem that Congress intended to prohibit the banks from arbitrarily fixing the amount to be charged for the service of collection and to require such banks to receive the checks and drafts at par, subject to such charges as the Federal Reserve Board may authorize.

In other words, the purpose of Congress appears to have been to vest in the Federal Reserve Board the power to fix exchange charges in all cases where the Federal reserve banks are used in making collections but to leave in the member banks the power to fix such charges when collections are made through their correspondents other than the Federal reserve bank of their district. This is clearly indicated by the provision above quoted which reads -

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"Nothing herein contained shall be construed as prohibiting a member bank from charging its actual expense incurred in collecting and remitting funds, or for exchange sold to its patrons."

Where member banks use their correspondents to make collections rather than to collect thrcugh the Federal reserve bank, the power to fix exchange charges is not vested in the Federal Reserve Board but is left to the member bank subject to the qualification that such charges must be limited to the actual expense incurred. Where, however, Federal reserve banks are used, the Federal Reserve Board is empowered to fix (a) the charges to be collected by the member bank from its patrons, and (b) the charge to be collected by the Federal reserve bank from the member bank whose checks are collected.

Respectfully,

(Signed) M. C. Elliott,

Counsel.

Hon. Charles S. Hamlin,
G O V E R N O R .

1/20/15.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

January 18, 1915.

Subject: Section 5200
Revised Statutes.

My dear Governor:

In response to your verbal request, I have carefully examined and considered the provisions of Section 5200 of the Revised Statutes of the United States, with the view of reaching a conclusion as to its proper interpretation. The language upon which you desire an opinion is as follows:

> "The total liabilities to any association, of any person .....for money borrowed .....shall at no time exceed one-tenth part of the amount of the capital stock of such association.....and one-tenth part of its unimpaired surplus fund.....<u>But the discount of bills of exchange drawn in good faith against actually existing values, and the discount of commercial or business paper actually owned by the person negotiating the same shall not be considered as money borrowed</u>".

From this it appears that the person discounting bills of exchange or commercial paper of the kind described, with a national bank, may become liable to the bank as a result of such transaction but such liability, under the terms of the Act, shall not be classed as "money borrowed". This liability may assume one of two forms, that is to say, it may result -

(a) from the discount of bills of exchange drawn in good faith against actually existing values, or

(b) from the discount of commercial or business paper actually owned by the person negotiating the same.

While such bills of exchange, or commercial or business paper, should represent the same class of transactions in order to be included in the exception quoted, it is necessary to consider them separately on account of their difference in form.

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Bills of Exchange.

In the case of bills of exchange drawn in good faith against actually existing values, the language "in good faith" is clearly intended to mean that the drawer must have the legal right to draw and that the bill of exchange must not be drawn merely with the hope or expectation that it will be paid.

The language "against actually existing values" is more vague and indefinite and less susceptible of clear interpretation. In reaching a conclusion as to its meaning we must consider the context of the Act in order to determine what class and character of transaction Congress had in contemplation. In doing so we find, as shown above, that the alternative form which such liability may assume is "commercial or business paper actually owned by the person negotiating the same". The term "commercial" as ordinarily used is defined to mean "pertaining to trade or commerce", that is to say, pertaining to buying and selling for money.

Considering this language, therefore, in its ordinary sense, it seems clear that Congress had in contemplation liabilities involved in the purchase and sale of commodities, and this view has been adopted and adhered to by the office of the Comptroller.

The question, therefore, arises whether "actually existing values" refers to the value of the commodity sold or can it be said to refer to the responsibility of the purchaser or drawee. The former view has been adopted by the office of the Comptroller as the more reasonable interpretation. This seems clearly justifiable (a) since it seems unlikely that Congress would have used the language "existing values" if it had intended to refer to the financial responsibility of an individual, firm or corporation, and (b) because the drawee against whom the bill is drawn is not legally bound to pay it until the bill is accepted. In other words, if the bill is excepted from the limitations of Section 5200 because the bank has recourse against some "existing values" and is not dependent solely upon the responsibility of the drawer or endorser who discounts it, the bank must be in a position to enforce its claim legally against whatever constitutes the "existing values" against which the bill is drawn and must, therefore, have a lien in some form evidenced by a bill of lading, warehouse receipt, or some other documentary evidence, for the commodity sold.

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Commercial or Business Paper.

In the case of "commercial or business paper actually owned by the person negotiating the same", the transaction must, as indicated, also be based upon the sale of some commodity, but in this instance the liability is evidenced in a form possessing characteristics distinctly different from that of a bill of exchange or draft. In other words, a draft or bill of exchange is merely an order on the drawee to pay and the drawee, as stated, is not legally bound until he accepts it.

On the other hand, when the liability involved is evidenced by the note of the purchaser, the purchaser assumes the primary or direct liability to the holder of the note and the bank discounting such note as an innocent purchaser for value without notice, takes it free from any equities existing as between the seller and the purchaser. The seller, as the endorser of the note, assumes only an indirect or contingent liability to the bank, which has recourse legally against the maker. In this case, therefore, the bank is not dependent solely upon the value of the commodity sold or upon the financial responsibility of the person discounting the note.

When the liability in question assumes the form of commercial or business paper, therefore, while the transaction, as stated, must be one in which the sale of a commodity is involved, it would seem to be unnecessary for the note to be accompanied by a bill of lading or warehouse receipt constituting a lien on such commodity. The only qualification contained in the statute in such case is that such "commercial or business paper" shall be actually owned by the person negotiating the same. In other words, there must have been an actual bona fide sale, and the debt due from the purchaser to the seller must actually exist when such "commercial or business paper" is discounted.

It has been contended that the sale of a commodity is not necessary in either case, on the ground that if the drawer of the bill of exchange has furnished money to the drawee, instead of sellijg the commodity, or if the payee of a note has made a loan to the maker, instead of making such sale, in either case, the drawer or the payee has furnished "existing values" and the draft or note, therefore, meets the requirements of the statute. There is, however, a distinction between a loan of money and the sale of a commodity. If a loan is made to a third party, evidenced by a note, it must be assumed that the proceeds of such loan are to be used for some purpose other than the payment of the

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note, since otherwise there would have been no occasion for the loan. In like manner, if the drawer of a bill of exchange furnishes funds to the drawee in advance, it must be assumed that such funds are to be used for some other purpose than the payment of the draft. Where commodities, however, are sold to the drawee or to the maker of the note, it is to be assumed that the drawee or maker intends to re-sell such commodities and to pay the draft or note with the proceeds.

Acceptances.

From the foregoing it will appear that where a bill of exchange drawn for the purchase price of a commodity sold, has been accepted by the purchaser or the drawee, it possesses the same characteristics as other commercial or business paper. That is to say, the purchaser thereupon assumes the direct or primary liability to the holder. The bank has recourse legally against the acceptor and holds the drawer and endorsers contingently liable in case the acceptor fails to pay such bill of exchange at maturity. In such case the acceptance, if actually owned by the person negotiating it, would seem to come within the broader language of "commercial or business paper actually owned by the person negotiating the same", and so need not be accompanied by a bill of lading, warehouse receipt, or other documentary evidence constituting a lien on the commodity sold.

Accommodation Paper.

If the bill of exchange is drawn merely on a promise on the part of the drawee to pay, or if the note is made merely to enable the holder to borrow money from the bank, such paper is in all respects accommodation paper, and while it may be said to conform in such case to the provisions of the Act, in so far as the form of liability is concerned, it lacks the elements necessary to remove it from the limitations imposed by Section 5200.

Finance or Investment Bills and Notes.

In like manner, if money is furnished merely for investment purposes, or for any purpose except to enable the purchaser to pay the seller for commodities purchased, the transaction could not be said to come within the exceptions to the limitations of Section 5200.

Court Decisions.

I have discussed at some length the various questions involved in the interpretation of this Act, in order

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to explain the reasons for the conclusions reached. There has been a considerable diversity of opinion as to the meaning of the language used, and so far as I have been able to learn, there has been no judicial construction of this Act by the United States courts which will assist in reaching a conclusion as to its meaning.

In a number of cases, where suit has been brought by national banks, the defense has been set up that loans made by such banks were in excess of the limitations of Section 5200 and, therefore, ultra vires. In such cases the courts have held that this does not invalidate the loan nor constitute a defense but is a matter merely of regulation. Accordingly, they have not construed the language in question but have held, in effect, that this question can best be raised in a suit to forfeit the charter of a national bank brought by the Comptroller of the Currency under authority of Section 5239 of the Revised Statutes. As no such suit has ever been instituted by the Comptroller, this question has not been judicially determined by the United States courts.

The question was considered, however, in the case of The Second National Bank of Oswego vs. Burt, 93 N. Y. 233, when in construing the proviso in Section 5200 which reads, "But the discount of bills of exchange drawn in good faith against actually existing values, and the discount of commercial or business paper actually owned by the person negotiating the same, shall not be considered as money borrowed", the Court said:

> "We think it entirely immaterial whether such bills are accompanied by a specific bill of lading in each case, or are drawn against property previously consigned, and existing either in its original form or in the shape of proceeds of sales in the hands of the consignees. In either case the funds have already been provided by the drawer in the hands of the drawees to meet the requirements of the obligation.
>
> "The object of this provision of the Currency Act was to guard national banks from the hazard of loaning money in improvident amounts upon speculative and accommodation paper, but it contemplated and permitted to an unlimited amount the discount of paper used and required in facilitating the transfer of property and money in the transaction of the legitimate business of the country."

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C. S. H. No. 6.

In this case the firm of Page & Company had drawn a bill of exchange against White & Company, another firm composed of the same members, who were the regular consignees for Page & Company in the sale of lumber. While the bill of lading did not accompany the bill of exchange, it appears that White & Company accepted the bill of exchange before it was discounted and so the bank had recourse against the drawee legally. The views herein expressed are therefore in accord with the decision of the court in this case, which appears to be the only reported decision of any court of competent jurisdiction dealing directly with this subject.

Summary of Conclusions.

To summarize the conclusions reached, I am of the opinion that any liabilities to a national bank contracted by any person, firm or corporation, are subject to the limitations of Section 5200, except -

(a) Liabilities evidenced by a bill of exchange drawn by the seller of some commodity against the purchaser and secured by bill of lading, warehouse receipt, or other documentary evidence giving the bank a lien on or recourse against the commodity in question.

(b) Liabilities evidenced by accepted bills of exchange drawn for the purchase price of commodities sold, such acceptances being actually owned by the person negotiating same.

(c) Liabilities evidenced by a note executed by the purchaser of a commodity for the whole or part of the purchase price, endorsed by the seller and discounted by the seller or actual owner of such note.

Respectfully,

(Signed) M. C. ELLIOTT

Counsel.

Honorable C. S. Hamlin,
Governor.

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Recommendations of the Committee on

STAFF AND ORGANIZATION

Filling Vacancies.

I.

In carrying out the previously expressed wish of the Board, the Committee on Staff recommends that appointments hereafter to be made by the Board, except in the case of heads of divisions and of technical experts when otherwise authorized, shall be made from the eligible list established by the examinations held December 9, 10, and 11, 1914.

Of 493 persons who took these examinations, a total of 236, or 48%, passed, classified as follows:

	Male	Female
Stenographer and Typewriter	15	47
Bookkeeper	5	--
Clerk	33	34
Messenger	37	11
Stenographer (only)	4	5
Typewriter (only)	12	33
	106	130

II.

In filling vacancies on the staff it is recommended that, for every vacancy, five applicants shall be certified in rotation from the top of the eligible list, from which one shall be selected by a committee consisting of a designated member of the Federal Reserve Board, the Secretary or the Assistant Secretary, and the head of the Division. The four rejected will be included in the next group of five to be certified, provided, however, that no applicant shall be certified more than three times, unless the above mentioned Committee considers that an injustice has been done and that a discarded employee should be again certified.

III.

In accordance with the previous action of the Board, all employees shall be appointed subject to a probationary period of sixty days and the head of the Division in which the employee is at work shall certify before the sixty days have expired that, in his opinion, the employee should be given a permanent appointment.

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IV.

(A) Those now employed in a temporary capacity, who have failed to pass the examination will be dropped from the service at the convenience of the Board.

(B) Those who have passed the examination with a rank of eighty percent (80%) or over may be continued in the service if needed, but not otherwise.

(C) If it is necessary permanently to fill positions which are now classed as temporary, they shall be filled from the ranks of those who, having passed examinations, are on the eligible list; provided, however, that employees who ranked as Grade "A" in the service of the Organization Committee and passed the examination of December 1914, but who were not included in the permanent staff on November 2, 1914, on account of there being no vacancies, shall be first certified.

F. A. Delano)
)
)
) Committee.
)
W. P. G. Harding)
)

Adopted by the Federal Reserve Board at its meeting
January 20, 1915.

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137.

Federal Reserve Agents are requested to examine the attached regulation and be prepared to make any suggestions which they have to make at the meeting to be held in Washington, February 1, 1915.

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FEDERAL RESERVE BOARD

Washington, January .., 1915.

ISSUE AND RETIREMENT OF FEDERAL RESERVE NOTES.

(1) Each Federal Reserve Agent from time to time and as far in advance as possible shall notify the Federal Reserve Board of the supply of Federal reserve notes he expects to require in order to meet applications for issue, stating the total amount of each denomination desired. (Form No.....)

(2) The Federal Reserve Board will determine to what extent Federal reserve notes shall be supplied the Federal Reserve Agents and will notify them of the amounts that they are authorized to issue from time to time to their respective banks in response to applications duly approved by said agents.

(3) The Federal Reserve Agent shall from time to time notify his Federal Reserve Bank of the extent to which he is authorized to meet applications for Federal reserve notes.

(4) The Federal Reserve Board will advise the Comptroller of the Currency of the requirements of each Federal Reserve Agent and will make requisition upon him for the shipment of the notes. The Comptroller of the Currency will advise the Federal Reserve Board of all receipts of completed Federal reserve notes from the Bureau of Engraving and Printing and all shipments to the Federal Reserve Agents.

(5) A Federal Reserve Bank desiring to issue Federal reserve notes shall make application therefor to its Federal Reserve Agent furnishing at the same time a list of the collateral which it proposes to tender as security for said notes. (Form No.....)

(6) The Federal Reserve Agent shall carefully examine the collateral offered and make such inquiries as he may deem necessary. If satisfied that the collateral conforms to the provisions of Section 13 of the Federal Reserve Act and the regulations of the Federal Reserve Board made pursuant thereto, he shall so inform the Federal Reserve Bank and shall notify said bank that Federal reserve notes will be supplied to it as soon as the collateral is deposited and the requisite gold redemption fund paid to the Treasurer of the United States at the Treasury Department in Washington or at any Subtreasury of the United States; (#) and the required gold reserve set apart by said bank.

(#) Note: Under Section 16 of the Federal Reserve Act this redemption fund may be increased above the 5% legal minimum at the discretion of the Secretary of the Treasury, and is to be included as part of the forty per centum reserve required to be held by the bank.

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(7) On receipt of said collateral and a certificate from the Treasurer of the United States or any Assistant Treasurer of the United States setting forth that the Federal Reserve Bank has deposited with him for the gold redemption fund the amount noted in the certificate, the Federal Reserve Agent, if said certificate of deposit is of the amount required for such redemption fund and if he is satisfied that the bank has in its vaults the gold reserve required by law to be held against such notes, shall issue to the extent that such issue has been authorized by the Federal Reserve Board, Federal reserve notes to said bank, receipting for said collateral (Form B.D.21-2), reporting to the Federal Reserve Board each day all notes issued to and withdrawn by said bank (Form F.R.A.5), and notifying said Board of the collateral accepted (Form B.D.21-3). The Federal Reserve Agent, upon issuing such notes, shall at once notify the Treasurer of the United States in order that he may be satisfied that the proper fund has been deposited in the Treasury for the redemption of such notes.

(8) If at any time the Federal Reserve Agent deems it necessary to require changes in either the character or amount of the collateral deposited to secure said notes, he shall notify the Federal Reserve Board and at the same time shall call upon the Federal Reserve Bank for additional or new collateral to be added to or substituted for that which in his opinion or in the opinion of the Federal Reserve Board is unsatisfactory. (Form No....)

(9) The Federal Reserve Agent shall compute and collect any graduated tax which may be imposed by the Federal Reserve Board, whenever said Board may permit reserve requirements below the Thirty-five per centum specified in Section 16 of said Act, reporting his action to the Federal Reserve Board, and at the same time depositing any sum so collected with the Treasurer of the United States, at the Treasury Department, at Washington, or at any subtreasury. A warrant will thereupon be issued covering said recepts into the Treasury.

(10) If at any time the gold reserve required by law to be held by a Federal reserve bank against Federal reserve notes issued to it falls below 40% (including therein the gold fund required to be maintained in the Treasury) the Federal Reserve Agent shall at once notify the Federal Reserve Board.

(11) The Federal Reserve Board will, upon receipt of notice of deficiency in gold reserve, establish a graduated tax upon such deficiency as provided in Section 11 of the Federal Reserve Act, which tax shall be computed and collected by the Federal Reserve Agent, reported to the Federal Reserve Board and deposited with the Treasurer of the United States at the Treasury Department in Washington, D.C., or at any Subtreasury, at the same time furnishing the Treasurer of the United States full particulars. A warrant will thereupon be issued covering said receipts into the Treasury. Said tax shall be computed as follows:

When reserves fall below 40% but are in excess of 32½%, the tax upon the deficiency shall be at the rate of 1% per annum;

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When reservesfall below 32½% but are in excess of 30%, the tax on the entire deficiency below 40% shall be at the rate of 2½% per annum;

When reserves fall below 30% but exceed 27½%, the tax upon the entire deficiency below 40% shall be at the rate of 4% per annum;

and so on, increasing at the rate of 1½% with each reduction in reserve amounting to 2½% or any fraction thereof.

Gold reserves against Federal reserve notes	Penalty tax on Deficiency in reserves.
40%	(Legal Minimum including Redemption Fund).
37½%	1%
35 %	1%
32½%	1%
30 %	2½%
27½%	4 %
25 %	5½%
22½%	7 %
20 %	8½%
17½%	10 %
15 %	11½%
12½%	13 %
10 %	14½%
7½%	16 %
5 %	17½%
2½%	19 %
0	20½%

(12) A Federal Reserve Bank upon application to its Federal Reserve Agent may exchange its notes that are unfit for circulation for those that are fit for circulation, or may exchange notes of one denomination for those of another. Any transaction in these respects will be reported to the Federal Reserve Board by the Federal Reserve Agent in the daily report of transactions in Federal reserve notes (Form No...)

(13) Any Federal reserve notes in the hands of a Federal Reserve Agent that are unfit for circulation shall from time to time be forwarded to the Comptroller of the Currency for cancellation and destruction (Form No.....). The notes to be returned shall be assorted by denominations and each one hundred notes or less inclosed in a paper strap marked with the amount. Each one thousand notes of each denomination, as nearly as convenient, in straps, shall be inclosed in a paper band likewise marked with the amount contained therein. Not to exceed four such bundles of not exceeding one thousand notes each shall be securely tied, wrapped and sealed, with a memorandum inclosed giving an inventory of the contents and the agent's name and bank (Form No...) and the package forwarded to the Comptroller of the Currency, Treasury Department, Washington, D.C., with charges prepaid. The Federal Reserve Agent shall send advice by mail to the Comptroller of the Currency and to the Federal Reserve Board of each

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shipment of unfit notes (Forms Nos....and.....). The Federal Reserve Agent will state in his daily report to the Federal Reserve Board the amount of unfit notes of each denomination in his possession.

(14) The Comptroller of the Currency after verification of such receipts of notes unfit for circulation will cancel the same by the method prescribed by the Secretary of the Treasury for United States paper currency retired through the Treasurer of the United States and will deliver one half of each note to the Secretary of the Treasury (Division of Loans and Currency) for independent verification. Report of such verification will be made by the Division of Loans and Currency to the Comptroller of the Currency and after any necessary adjustments have been made the separate halves of the canceled notes will be delivered by the Comptroller of the Currency and by the Division of Loans and Currency to the destruction committee for disposition in the usual manner, and the Federal Reserve Agent will be given credit on the books of the Comptroller of the Currency for the notes so destroyed. The Comptroller of the Currency will advise the Federal Reserve Board of all unfit notes canceled and destroyed (Form No.,...).

(15) The Federal Reserve Board will maintain a record of the amounts of notes of the several denominations in the reserve stock in the office of the Comptroller of the Currency, of the amounts supplied to each Federal Reserve Agent, of the amounts issued through said agents to their respective banks, and of the amounts of fit and unfit notes at all times in the possession of each agent.

(16) Whenever Federal reserve notes issued by one Federal Reserve Bank shall be received by another Federal Reserve Bank they shall immediately be returned to the issuing bank for credit or redemption.

(17) Upon the receipt of notice from the Federal Reserve Board that a rate of interest has been established to be charged upon issues of Federal reserve notes, the Federal Reserve Agent shall notify his bank and shall compute and collect the amount of interest due from said bank, report the same to the Federal Reserve Board and deposit the collection with the Treasurer of the United States at the Treasury Department in Washington or at any Subtreasury, at the same time furnishing the Treasurer of the United States full particulars. A warrant will thereupon be issued covering said receipts into the Treasury.

(18) A Federal Reserve Bank desiring to reduce its liability for outstanding Federal reserve notes may deposit with the Federal Reserve Agent gold, gold certificates, or lawful money of the United States (i.e. legal tender coin (gold or silver), legal tender notes, gold certificates or silver certificates), and thereupon the Federal Reserve Agent shall return to the Federal reserve bank a proportionate amount of collateral deposited as security for the notes, the transaction to be reported to the Federal Reserve Board by the Federal Reserve Agent. The Federal Reserve Agent shall decline to receive such deposits unless and until any Federal reserve notes held by said bank as cash are surrendered.

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(19). The Federal Reserve Agent shall hold such deposits of gold, gold certificates or lawful money of the United States subject to the order of the Federal Reserve Board. With the consent of the Secretary of the Treasury obtained through the Federal Reserve Board the Federal Reserve Agent may deposit any gold or gold certificates contained in such deposits with the Treasurer of the United States at the Treasury Department in Washington or with any Assistant Treasurer of the United States and receive therefor gold certificates payable to the order of the Federal Reserve Agent. On depoait of such notes, gold, gold certificates or lawful money, a proportionate amount of the collateral may be returned to said bank, the transaction to be reported at once to the Federal Reserve Board, using for that purpose Form F.R.A.5.

(20) When a Federal Reserve Bank deposits its Federal reserve notes with the Federal Reserve Agent for retirement, the agent shall return to the bank a proportionate amount of the collateral securing the notes, or if the collateral previously has been returned upon the deposit of gold, gold certificates or lawful money of the United States, a proportionate amount of such deposits shall be returned except in the case that the gold deposits have been required by the Federal Reserve Board at the request of the Secretary of the Treasury to be deposited with the Treasurer of the United States for redemption purposes.

(21) Upon receipt of notice from a Federal Reserve Agent that certain Federal reserve notes have been retired, the Federal Reserve Board will advise the Treasurer of the United States of such retirements and will request the Secretary of the Treasury to instruct the Treasurer of the United States to return to the Federal Reserve Bank such portion of its redemption fund as may be in excess of the minimum amount required to be maintained in the Treasury of the United States against its notes still outstanding.

(22) When Federal reserve notes have been returned for retirement by the Federal Reserve Bank to which issued the notes shall be held by the Federal Reserve Agent and shall be reissued only on the same terms as an original issue, except that any notes in hand may be used for the purpose of replacing notes unfit for circulation or of exchanging one denomination for another, as provided in Section 11 of these regulations.

(23) When a Federal Reserve Bank shall exercise its right to withdraw collateral and substitute therefor other collateral against Federal reserve notes, the Federal Reserve Agent shall examine said substitute collateral and pass upon it in exactly the same way as if it were collateral for an original issue of Federal reserve notes. If

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approving the collateral, he may make the exchange, reporting the fact at once to the Federal Reserve Board (Form B.D. 28-3).

(24) Federal reserve notes presented to the Treasurer of the United States in Washington for redemption shall be redeemed from the redemption fund and returned to the issuing bank, and thereupon the issuing bank shall reimburse the Treasurer of the United States for the redemption fund in like amount.

(25) Federal reserve notes received in the Treasury of the United States otherwise than for redemption may at the discretion of the Secretary of the Treasury be redeemed and returned to the issuing bank for reimbursement of the redemption fund with the Treasurer of the United States, or they may be returned to the issuing bank for the credit of the United States, or with the consent of the Federal Reserve Board, they may be paid out by the Treasurer in usual course of business.

(26) The Treasurer of the United States will furnish a daily report to the Federal Reserve Board giving detailed information regarding his transactions in Federal reserve notes.

(27) At the close of business each month each Federal Reserve Agent will furnish the Federal Reserve Board with a consolidated statement of all transactions in Federal reserve notes during the month showing for each denomination the number of notes on hand at the beginning of the month; the number received from the Comptroller of the Currency during the month; the number returned by the Federal Reserve Bank; the number issued to the Federal Reserve Bank, the number returned to the Comptroller of the Currency for cancellation and destruction and the number on hand at the close of the month. The same report will show the total amount of notes in circulation at the end of the month, the total amount of each kind of money of the United States in hand for retirement of the notes, and the amount of gold reserve, other than the redemption fund deposited with the Treasurer, held by the bank.

1/23/15.

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Suggested form of bill authorizing
State banks to become members of the Federal Reserve System.

A BILL to authorize State banks and trust companies incorporated under the laws of this State to subscribe to the stock and become members of the Federal reserve banks created and organized under an Act of Congress of the United States approved December 23, 1913, and known as the Federal Reserve Act, and to authorize the State authorities to accept examinations and audits made pursuant to the provisions of said Act of Congress in lieu of examinations required by the laws of this State.

Be it enacted, etc., That any bank or trust company incorporated under the laws of this State shall have power to subscribe to the capital stock and become a member of a Federal Reserve Bank created and organized under an Act of Congress of the United States approved December 23, 1913, and known as the Federal Reserve Act, and shall have power to assume such liabilities and to exercise such powers as a member of such Federal Reserve Bank as are prescribed by the provisions of said Act, or amendments thereto, and so long as such bank shall remain a member of the Federal Reserve System created by said Act of Congress it shall be subject to examination by the legally constituted authorities and to all provisions of said Federal Reserve Act and regulations made pursuant thereto by the Federal Reserve Board which are applicable to such banks as members of the Federal Reserve System, and the State authorities may, in their discretion, accept examinations and audits made under the provisions of the Federal Reserve Act in lieu of examinations required of banks organized under the laws of this State.

1/26/15.

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January 25, 1915.

My dear Governor:

I have your letter of the ninth instant enclosing, as stated, copy of letter from Mr. Alfred L. Ripley, First Vice President of the Merchants National Bank of Boston, asking for an opinion as to whether acceptances of a national bank under Section 13 of the Federal Reserve Act should be construed as borrowed money within the meaning of Section 5200 of the Revised Statutes.

Section 5200 reads as follows:

> "The total liabilities to any association, of any person ..... for money borrowed .....shall at no time exceed one-tenth part of the amount of the capital stock of such associations, actually paid in and unimpaired, and one-tenth part of its unimpaired surplus fund. . . But the discount of bills of exchange drawn in good faith against actually existing values, and the discount of commercial or business paper actually owned by the person negotiating the same shall not be considered as money borrowed."

When this Act was passed, national banks were not permitted to accept drafts or bills of exchange drawn against them, but Section 13 of the Federal Reserve Act provides that -

> "Any member bank may accept drafts or bills of exchange drawn upon it and growing out of transactions involving the importation or exportation of goods having not more than six months sight to run; but no bank shall accept such bills to an amount equal at any time in the aggregate to more than one-half its paid-up capital stock ans surplus."

It is, of course, assumed that where a member bank accepts a draft or bill of exchange for a customer, the acceptance is discounted by a third party and not by the accepting bank. The legal effect of such an acceptance is

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for the bank to become primarily liable and to obligate itself to pay the draft or bill of exchange at maturity. The acceptance is, therefore, a loan of the bank's credit rather than a loan of money by the bank. The liability of the drawer is contingent and not direct.

In an opinion rendered to the Secretary of the Treasury by Attorney General Benjamin Harris Brewster, this subject was treated by analogy in dealing with the question of the certification of checks by national banks. In that opinion the Attorney General, quoting from the case of Security Bank vs. National Bank (67 N. Y., 462), said:

> "The manifest object of the certification is to indicate the assent of the certifying bank to the request of the drawer of the check that the drawee will pay to the holder the sum mentioned; and this is what an acceptor does by his acceptance of a bill."

In the opinion referred to the Attorney General considers three questions, the second of which is as follows:

> "(2) If a national bank has the power to make such an acceptance, would such acceptance at a time when the money was not on deposit to the credit of the drawer by a liability to it for money borrowed, and as such be required to be limited to one-tenth of the paid-in capital of the bank, as provided by Section 5200, Revised Statutes?"

In dealing with this question the Attorney General says:

> "The case presented in the second question is not, in my opinion, covered by the provisions of section 5200, Revised Statutes.
>
> "The restriction there applies only to liabilities 'for money borrowed'. The acceptance of a check, where the drawer has no funds on deposit, would be a loan of the credit of the bank rather than loan of money, and, if otherwise unobjectionable, it could not properly be regarded as within the terms of the restriction adverted to".

As stated, the certification of a check where the depositor has no funds to his credit, is prohibited by statute, but the acceptance of a bill of exchange drawn upon

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a member bank which grows out of transactions involving the importation or exportation of goods, is, under the conditions prescribed in Section 13, now permitted; and, following the reasoning adopted by the Attorney General in the case referred to, it would seem that such acceptance does not come within the limitations of Section 5200.

The transaction must, however, be entered into in good faith, and the acceptance by the member bank must comply in all respects with the provisions of Section 13.

Respectfully,

Honorable C. S. Hamlin,
Governor.

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CONFIDENTIAL.

ADOPTED BY THE FEDERAL RESERVE BOARD

AT A MEETING HELD ON FEB. 1, 1915.

Amendments to the Board's by-laws, notice of the offering of which had already been given in due form, were read to the Board and on motion approved, as follows:

AMENDMENT I

Section 5 of Article 11 of these By-laws is hereby amended to read:

> "The Secretary shall have custody of the seal and shall have power to affix the same to all instruments requiring it under the authority of the Board. Such instruments shall be attested by the Secretary."

AMENDMENT II.

The Board shall appoint an Assistant Secretary, who shall exercise the powers and discharge the duties of the Secretary in his absence or disability and shall perform such other duties as may be assigned to him from time to time by the Board, or by the Secretary of the Board.

AMENDMENT III.

Section 1. The Board shall appoint a Fiscal Agent whose duty it shall be to collect and deposit all moneys receivable by the Board with the Treasurer of the United States, to be placed in a Special Fund established on the books of the Treasury for the Federal Reserve Board.

Section 2. The Fiscal Agent shall execute a bond with surety satisfactory to the Board in a sum to be fixed by the Board.

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Section 3. Payment of expenses and other disbursements of the Board shall be made by the Fiscal Agent, upon proper vouchers, out of the moneys advanced to him by requisition and warrant out of the Special Fund and placed to his official credit with the Treasurer of the United States, as provided by Section 5 of this amendment.

Section 4. The Fiscal Agent shall prepare a monthly account in such form as shall be approved by the Comptroller of the Treasury, and, after approval by the Governor, such monthly account shall be submitted to the Auditor for the State and other Departments.

Section 5. The Governor shall, when necessary make requisition on the Treasurer of the United States for the advance of such sums to the Fiscal Agent as may be necessary from the Federal Reserve Board Fund.

AMENDMENT IV.

So much of the provisions of the By-laws heretofore adopted inconsistent with Amendments I, II, and III are hereby repealed.

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144 a.

February 2, 1915.

SUBJECT: Conditions attached to bills of exchange and acceptances affecting negotiability.

My dear Governor:

I have the honor to acknowledge receipt of your request for an opinion on the subject of conditions attached to bills of exchange and acceptances which affect their negotiability.

It is somewhat difficult to define in specific terms what conditions may or may not be prescribed in a bill of exchange without affecting the negotiability of such bill since the negotiable instruments laws of all the states are not identical and the decisions of the various courts are by no means uniform on this subject.

As I understand it, the Board has under consideration the question of prescribing a method by which bills of exchange or acceptances dealt in by member banks or Federal reserve banks may show that such bills or acceptances grow out of transactions involving the exportation or importation of goods without affecting their negotiability, and it is primarily upon this question that you desire an opinion.

In dealing with this subject, it is important to keep in mind the distinctive difference between a bill of exchange and an acceptance, and also the difference in status between an acceptor and a drawer of a bill.

Section 126 of the negotiable instruments law adopted by forty-one states and the District of Columbia, defines a bill of exchange 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 on demand or at a fixed or determinable future time a sum certain in money to order or to bearer".

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Section 127 states that -.

"A bill of itself does not operate as an assignment of the funds in the hands of the drawee available for the payment thereof, and the drawee is not liable on the bill unless and until he accepts the same".

Until the bill is accepted, therefore, the drawer is primarily liable and the bank discounting such bill can have recourse only against the drawer or a prior endorser in the event that the drawee declines to accept such bill when presented.

On the other hand, acceptance is defined by Section 132 of the negotiable instruments law as -

"The signification by the drawee of his assent to the order of the drawer. The acceptance must be in writing and signed by the drawee. It must not express that the drawee will perform his promise by any other means than the payment of money".

When a bill has been accepted, the acceptor becomes primarily liable and the contract of the drawer is substantially changed to that of endorser.

It will be observed from the foregoing that a bill of exchange, in order to be negotiable, must not only be payable to order or bearer, so that title may be transferred by the holder, but it must also be an unconditional order to pay in money.

A conditional acceptance is defined in 4 Am. & Eng. Encl. of Law, 224, as an undertaking by a drawee to pay, dependent, however, upon the performance or happening of a stipulated condition or contingency. But as shown later, a general acceptance of a conditional bill is also in effect a conditional acceptance. The terms, therefore, both of the order to pay, as indicated by the bill of exchange when drawn, and the acceptance as indicated by the language used by the acceptor, must be free from qualifications or conditions if the bill or acceptance is to retain in all respects its negotiability and to be free from equities existing between the drawer and the drawee or the acceptor. This being true, the question arises as to what form may be used to show the transaction on which the acceptance is based without destroying its negotiability.

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The Federal Reserve Act provides that such bills or acceptances must grow out of transactions involving the exportation or importation of goods. It is to be assumed, therefore, that ultimately the proceeds of the sale of the goods imported or exported are to be used to extinguish the debt evidenced by the acceptance. To avoid any question of negotiability, however, neither the bill as drawn nor the acceptance made must be in terms to indicate that the payment is to be confined to such proceeds. As stated by Norton, on Bills and Notes, Third Edition, Page 138, -

> "The true test is whether the drawee is confined to the particular fund, or whether, though a particular fund is mentioned, the drawee may charge the bill up to the general account of the drawer if the designated fund turn out to be insufficient. It must appear that the bill of exchange is drawn on the general credit of the drawer. It must carry with it the personal credit of the drawer, not confined to any fund".

This being true of a bill of exchange, the question arises whether or not the contract of acceptance is wholly independent of the terms contained in the bill. The cases and authorities all agree that a general acceptance of a bill of exchange is an undertaking on the part of the drawee to pay the bill absolutely according to its tenor.

4 Am. & Eng. Encl. of Law 207.
English Bills of Exch., Act, Sec. 17.
Cox v. National Bank, 100 U. S. 712
Bailey on Bills (2nd Am. Ed.) 154.

Consequently if the bill orders payment out of a particular fund, a general acceptance thereof is an undertaking to pay out of that fund and no more, and it is, therefore, a conditional acceptance, though general in form.

Hoagland v. Erck, 11 Neb. 580.
Newhall v. Clark, 3 Cush. (Mass) 376.
Smith v. Wood, 1 N. J. Eq. 74.
Cook v. Wolfendale, 105, Mass., 401.

It is to be remembered, of course, that an acceptance may be conditional and therefore non-negotiable, even though the bill itself was unconditional, if the terms in the contract of acceptance specify that payment is to be made out of a particular fund or is dependent upon the hap-

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pening of a certain contingency. As Justice Clifford stated in Cox v. National Bank, supra, "An acceptance is an engagement to pay the bill according to the tenor of the acceptance and * * * a general acceptance is an engagement to pay according to the tenor of the bill."

The difficult question, however, is to construe the words used, to apply the test given in Norton, to determine whether in fact the acceptance is conditional; or, more specifically, to determine whether the drawee is confined to a particular fund merely by a reference on the bill or in the acceptance to that fund. It is a question for the court to determine in each individual case, because, the facts being proved or admitted, the question whether an undertaking is a conditional acceptance is a question of law for the court to decide. Sproat v. Matthews 1 Term. R. 182.

It was held in Corbett v. Clark, 45 Wis., 403, that an order to "pay C. A. Corbett $183 and take the same out of our share of the grain" was an unconditional bill and a general acceptance thereof also unconditional. The court held that this was a mere direction as to the fund out of which the drawee was to reimburse himself. In Redman v. Adams, 51 Maine, 433, where the words of the bill were "charge the same against whatever amount may be due me for my share of fish caught on board schooner 'Morning Star' ", and the acceptance was general, the court held that this was a mere reference to the fund to call the attention of the drawee to his means of reimbursement.

The great majority of cases incline to the view that the presumption is in favor of an unconditional order and unless the direction on the bill or acceptance clearly and expressly directs payment to be made out of a certain fund, the court will consider it merely as a reference to the mode of reimbursement rather than an absolute restriction to the particular fund mentioned.

In a case decided in May, 1911, by the United States Circuit Court for the Southern District of New York (Hannay vs. The Guaranty Trust Company, 187 Fed. 686.) it was held that "Value received and charge the same to the account of 100/RSMI bales of cotton" written on a draft made it conditional because it limited payment to the proceeds of this particular cotton. The draft having been held to be conditional a general acceptance thereof was also held to be conditional. It is true that this decision was reversed in the United States Circuit Court of Appeals in 210 Fed. 810, but on the ground that the English instead of the American law applied to this particular transaction and without any attempt on the

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part of the court to decide whether the lower court was right or wrong under the American law. Thus it is seen how difficult it is to determine how a court will rule on any specific case. The rule or test is always the same, but whether the facts are within or without the rule is merely a matter of opinion. Extreme cases are easy to decide but as the cases verge toward the center, the line of demarcation becomes hazy and difficult of determination.

It would seem, therefore, that Federal reserve banks and member banks should consider carefully the risk involved in discounting bills of exchange or acceptances which in terms indicate any particular fund or any particular property out of which payment of the draft is to be made, because of the doubt as to the construction that might be put upon such an acceptance. It would be far more prudent to require that the directions in a bill of exchange be to pay in money and to charge to the account of the drawer, without any qualification as to any particular fund. There is no doubt, however, that a reference, in general terms, on the face of a bill to the fact that it is based on the importation or exportation of goods would not make it conditional and non-negotiable.

Respectfully,

(Signed) M. C. ELLIOTT.

Counsel.

3/6/15/

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STATEMENT FOR THE PRESS.

FEBRUARY 5, 1915.

The Federal Reserve Board today announced that a joint conference between the Board and the Federal Reserve agents of the several banks, lasting since Monday last, had been brought to a close. The Federal Reserve Agents have been in practically continuous session every day since their arrival in the City, three joint conferences having been had with the Federal Reserve Board itself.

The Board at the first conference presented to the Federal Reserve Agents a list of questions touching the conduct and operation of the Federal Reserve System and the relations of the Federal Reserve Banks with their members, on which it desired to ascertain their views. Practically all of these topics were considered during the deliberations and various memoranda were prepared by committee of the Reserve Agents and a formal report is in preparation.

The Federal Reserve Agents presented a report setting forth the several definite steps which in their judgment should be taken in developing the clearing functions of the Federal Reserve Banks, both as regards clearings within the several districts and clearings between the several districts. Among other topics covered were the bonding of Federal Reserve agents, methods of improving the plans for the issue of currency, the situation at the different banks and a variety of other topics. Each Federal Reserve agent was asked to express his opinion with reference to business prospects in the several districts, and nearly all were optimistic with regard to the probable business of the coming year and the chances of profitable operations by Federal reserve banks. Some agents reported that the banks were already fully providing for expenses and a share of their dividends, while in practically all districts it appeared that the support of member banks was being obtained and that the prospect of successful cooperative work was favorable.

The meeting was reported highly harmonious and was considered productive of beneficial results. It is the first that has been held since the convention of officers and directors of reserve banks held on October 20-22, for the purpose of establishing plans for the opening of the new institutions.

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FEDERAL RESERVE BOARD

Washington

February 5, 1915.

My dear Governor:

In the accompanying letter Mr. McDougal asks for an expression of opinion on the subject of whether or not a national bank which is a member of the Federal Reserve System may make loans on real estate which is not situated in the district in which the national bank is located.

In reply I beg to advise that Section 24 of the Federal Reserve Act provides in terms that -

> "Any national banking association not situated in a central reserve city may make loans secured by improved and unencumbered farm land, situated within its Federal reserve district .....The Federal Reserve Board shall have power from time to time to add to the list of cities in which national banks shall not be permitted to make loans secured upon real estate in the manner described in this section."

Section 5137 of the Revised Statutes provides that national banking associations may purchase, hold and convey real estate for certain specific purposes and for no others. The effect of Section 24 of the Federal Reserve Act is to extend the powers granted by Section 5137 and since this Act specifically limits loans to those secured by farm land situated within the district in which the bank is located, it is obvious that the Federal Reserve Board is without power by regulation to vitiate this restriction.

Respectfully,

(Signed) M. C. ELLIOTT

Counsel.

Hon. Charles S. Hamlin,
Governor.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

February Fourth
Nineteen Fifteen.

My dear Governor:-

I have the honor to acknowledge receipt of letter from Mr. Theodore Wold, Governor of the Federal Reserve Bank of Minneapolis, dated December 21, 1914, addressed to the Federal Reserve Board and referred to this office by the Secretary to the Board.

Mr. Wold desires an interpretation of that part of Section Thirteen of the Federal Reserve Act which reads as follows:

> "The aggregate of such notes and bills bearing the signature or indorsement of any one person, company, firm or corporation rediscounted for any one bank shall at no time exceed ten per centum of the unimpaired capital and surplus of said bank; but this restriction shall not apply to the discount of bills of exchange drawn in good faith against actually existing values".

Mr. Wold inquires particularly as to what, in the opinion of the Board, constitutes a "bill of exchange drawn in good faith against actually existing values", and asks whether this language would include a note maturing within ninety days given in payment of a carload of sugar, or some other commodity.

Under date of January 18, 1915, this office filed with the Board an opinion on Section 5200 of the Revised Statutes and considered in detail the language used in this Section which reads as follows:

> "But the discount of bills of exchange drawn in good faith against actually existing values and the discount of commercial or business paper actually owned by the persons negotiating the same, should not be considered as money borrowed".

It will be observed that in Section Thirteen referred to by Mr. Wold Congress has incorporated only the first exception contained in Section 5200 of the Revised

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Statutes - that is to say, it provides that "this restriction shall not apply to the discount of bills of exchange drawn in good faith against actually existing values". It does not include in this exception the discount of commercial or business paper actually owned by the persons negotiating the same.

There is another important distinction between the language used in Section 5200 Revised Statutes and that used in Section 13 of the Federal Reserve Act. In the former case the statute provides that "the total liabilities to any person.....for money borrowed shall not exceed one tenth part of the capital etc.", while in Section 13 the more specific language is used that "the aggregate of such notes and bills bearing the signature or endorsement of any one person.....shall at no time exceed ten per centum" etc. Under this language the liabilities of the endorser as well as those of the maker and drawer of bills are expressly limited to ten per cent of the unimpaired capital and surplus of the applying bank when presented for rediscount.

In other words, Section 5200 contemplates that one person may become contingently liable to a national bank in excess of ten per cent of its capital and surplus under certain conditions, which liability may be evidenced by endorsement of commercial or business paper, and that such liability need not be classed as borrowed money. Under the more specific language of Section 13, however, this contingent liability represented by endorsement is precluded.

Without reviewing in detail the discussion contained in the opinion referred to, dated January 18, 1915, I am unable to reach the conclusion that any liabilities are excluded from the provisions of Section 13 above quoted except bills of exchange drawn in good faith against actually existing values - that is to say, liabilities evidenced by a bill of exchange drawn by the seller of some commodity against the purchaser and secured by bill of lading, warehouse receipt, or other documentary evidence giving the bank a lien on or recourse against the commodity in question.

Respectfully,

(Signed) M. C. ELLIOTT.

Counsel.

Hon. Charles S. Hamlin,
Governor.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

February 9, 1915.

My dear Governor:-

The following questions have been referred to this office by the Board for an opinion:

(1) Under Regulation F-I-(c)-3, does the term "taxable property" include franchises where such franchises are actually taxed upon the valuation set forth in the city's return of taxable property?

(2) Under Section 14 of the Federal Reserve Act, sub-section (b) where the Federal reserve bank is authorized to "buy and sell.....bills, notes, revenue bonds and warrants with a maturity from date of purchase of not exceeding six months", does this language permit the purchase of bonds having long maturities but which are acquired by a Federal reserve bank within six months of the date of maturity and, if so, under what circumstances may such purchases be made?

In answer to question (1), Regulation F reads in part as follows:

"I. A Federal Reserve Bank may purchase such warrants as are issued by a municipality.....
(c) 3. Whose net funded indebtedness does not exceed ten per centum of the valuation of its taxable property, to be ascertained by the last preceding valuation of property for the assessment of taxes".

This provision is not contained in the statute but is a matter of regulation and the language to be construed is accordingly that of the Board and it is within its discretion to determine whether or not the term "taxable property" shall include franchises.

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C. S. H. No. 2.

The courts have generally construed a franchise to be property subject to taxation and so giving the language "taxable property" its ordinary interpretation it would seem clear that franchises which are actually taxed and which are included in the city's return of taxable property should be taken into consideration in determining the net funded indebtedness as provided in Regulation F.

In the case of The West River Bridge Company vs. Dix et al, 6 How. (U. S.) 507-533, the Court said

> "A franchise is property, and nothing more; it is incorporeal property, and is so defined by Justice Blackstone, when treating, in his second volume, chap. 3, page 20, of the Rights of Things".

In the case of Society for Savings vs. Coite, 6 Wall (U. S.) 594-606, the Court holds that the franchise of a private corporation is a legitimate subject of taxation. This doctrine is affirmed in the case of Provident Institution vs. Massachusetts, 6 Wall (U. S.) 611-623 and again in the case of Hamilton Company vs. Massachusetts, 6 Wall, (U. S.) 632-638.

In answer to the second inquiry submitted, the Act provides that "revenue bonds.....with a maturity from date of purchase of not exceeding six months" may be purchased. The provision that such bonds must mature within six months from the "date of purchase" clearly indicates that Congress contemplated that such bonds might have a maturity of longer than six months at the date of issue.

It is true that the term "revenue bonds" is sometimes construed to refer to short-term bonds or warrants issued by municipalities to defray expenses for a short period prior to the collection of taxes.

The word "revenue", however, does not of itself limit the term of a bond to that of a fixed maximum maturity but instead refers to the character or nature of the bond rather than to the time of its maturity.

In other words, giving the language its ordinary interpretation, it would seem merely to indicate bonds of any maturity, payment of which is guaranteed out of the collection of taxes or assured revenues.

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C. S. H. No. 3.

The Act specifically provides that such bonds must be issued in anticipation of the collection of taxes or assured revenues but does not prescribe how long in advance of collection of such taxes the bonds may be issued. The provisions of the Act would seem to be complied with if, at the time of issue, provision is made for the establishment of a redemption or sinking fund which will be sufficient and available for the payment of the bonds at maturity and are, therefore, self-liquidating at the expiration of six months.

It is, of course, understood that all other provisions of Regulation "F", Series 1915, must be complied with before such bonds may be purchased.

In this connection, I beg to call attention to Paragraph VI, Regulation "F", which is as follows:

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

The Board has ruled that where such opinions have been procured and approved by counsel for a Federal reserve bank, any other Federal reserve bank shall be deemed to have complied with the requirement of this paragraph if it secures certified copy of such opinion and approval.

In order to avoid duplication of work I would, therefore, respectfully suggest that where such opinions have been procured and approved by counsel for a Federal reserve bank copy should be filed with the Federal Reserve Board so as to be available for other counsel who are called upon to pass upon the legality of the same issues.

Respectfully,

(Signed) M. C. ELLIOTT

Counsel.

Hon. Charles S. Hamlin,
Governor.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

227

February 15th, 1915.

My dear Governor:-

The attached letter from the Cashier of the National Bank of Flint, Flint, Michigan, raises the following questions:

(1) Does a note with waiver of demand, notice and protest on the back thereof, over the names of all the endorsers, require protest?
(2) What effect has waiver of demand, notice and protest printed on the face of a note?

Section 110 of the Negotiable Instruments Law, which is in force in forty-one states and the District of Columbia, provides that -

"Where the waiver is embodied in the instrument itself, it is binding upon all parties; but where it is written above the signature of an endorser, it binds him only".

In those states which have adopted this law, question number one should be answered in the affirmative since if the note contains the name of more than one endorser it will require protest to prevent the release of all endorsers except the one whose signature immediately follows the waiver.

This appears to be the safer course, also, in those states which have not adopted the Negotiable Instruments Law, since this rule was very generally followed by the courts prior to the adoption of this law by the States. Missouri and a few other states held to the contrary in some instances but the better view, which is sustained by the weight of authority, appears to be that a waiver of demand, notice and protest on the back of a note applies only to the endorser whose signature immediately follows such waiver.

In answer to question number two, it seems clear that where the waiver is printed on the face of a note it becomes a part of the contract and applies to all endorsers without reference to their position on the note.

Respectfully,

Hon. Charles S. Hamlin,
Governor.

(Signed) M.C.ELLIOTT,
Counsel.

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UNITED STATES CIVIL SERVICE COMMISSION

Washington, D. C.

February 19, 1915.

Hon. Charles S. Hamlin,

Governor, Federal Reserve Board,

Washington, D. C.

Sir:

This Commission has the honor to acknowledge the receipt of your communication of February 16, asking whether an employee of the Government appointed under the civil service rules who resigns from such employment to become a member of the staff of the Federal Reserve Board would thereby lose his civil service status.

Civil Service Rule X, clause 3, provides that "Any person may be retransferred to a position in which he was formerly employed, or to any position to which transfer could be made therefrom, if since his transfer he has been continuously in the executive * * * civil service of the United States * * * * * *."

The Federal Reserve Act, section 11, providing that employees shall be appointed without regard to the civil service act declares that "nothing herein shall prevent the President from placing such employees in the classified service." This provision, together with the reasons given in the opinion of the Attorney General made public December 19, 1914, indicate that an employee transferred to the Board from the classified service may be regarded for the purposes of the rules and in the interests of good administration as

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eligible for return to the classified service, to the position in which he was formerly employed or to any position to which transfer could be made thereform, if he has been continuously in the service.

It is suggested that your Board request this Commission to issue its certificate for the transfer in order that there may be a record in the Commission.

It may be added that in being transferred from the classified competitive service to the Federal Reserve Board, which is outside the classified service, the employee would not carry with him any other rights or privileges than those of reinstatement and retransfer. He would not, any more than any other employee of the Board, be entitled to charges and an opportunity of reply before removal as required by law in the case of competitive employees. The act makes it discretionary with the President to place employees of the Board in the classified service, and until he so directs, such employees acquire none of the rights and privileges attaching to classified employees except where transferred from the classified competitive service and then only to the extent of reinstatement or retransfer.

By direction of the Commission:

Very respectfully,

(Signed) JOHN A. McILHENNY,

President.

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EXAMINATION OF STATE BANKS AND TRUST COMPANIES

The Federal Reserve Board on February 10, 1915, adopted the following plan for the examination of State Banks and Trust Companies.

1 - Initial Examination of applying Bank -

A - Where State examinations are considered competent, after each examination a copy of examiner's report including either the text or a short digest of the text should be sent to the Federal Reserve Agent of the district in which the applying bank is situated and by him forwarded together with the application and its recommendation, to the Federal Reserve Board.

B - In States where examinations by State authorities are not considered to be of a sufficiently high standard to be acceptable to the Board, the initial examination of the applying institution, should be made by either an examiner designated by the Board or one suggested by the Federal Reserve Agent and approved by the Board or by a National Bank Examiner assigned by the Comptroller of the Currency at the request of the Board.

2 - State Banks which have been admitted to Membership -

A - Examinations made by State authorities who maintain a satisfactory standard, should be accepted by the Board - In such cases, arrangement should be made to have duplicate copies of examiners' report, including the text, sent to the Federal Reserve Agent of the district and by him forwarded to the Federal Reserve Board, one copy to be filed, and the second delivered to the Comptroller of the Currency.

B - In States where examinations by State authorities are not considered to be of sufficiently high standard, in order to prevent any claim of discrimination, authorization of acceptance of examinations might be given, but the Board should direct the holding of a special examination of State Member Banks, which are located in such States, at least once each year, either by examiners appointed by the Board, examiners designated by the Federal reserve bank, with the approval of the Board, or by National Bank Examiners, assigned by the Comptroller of the Currency at the request of the Board.

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FEDERAL RESERVE BOARD

WASHINGTON

February 24, 1915.

Subject: Statute of the State of California prohibiting soliciting of savings accounts.

My dear Governor:

The action of Mr. W. R. Williams, Superintendent of Banks of the State of California, in serving notice on certain national banks that he will seek to have imposed the penalties imposed by the California law for soliciting savings accounts, has been referred to this office for attention.

It appears that Section 49 of the Bank Act of the State of California provides as follows:

> "It shall not be lawful for any commercial bank, individual, trust company, association, firm, stock company, copartnership or corporation, to advertise or put forth a sign as a savings bank, either directly or indirectly or in any way to solicit or receive deposits or to transact business in the way or manner of a savings bank, or advertise that he or it is receiving or accepting savings, or in any way which might lead the public to believe that such deposits are received or invested under the same conditions or in the same manner as deposits in savings banks, except in the case of savings banks or banks having savings departments, subject to the provisions of this act. Any commercial bank, individual, trust company, association, firm, stock company, copartnership or corporation, violating any provision of this section shall forfeit to this state one hundred dollars a day for every day during which such violation continues."

The question arises whether or not the provisions of this Act can be made to apply to national banks doing business within the State of California.

It does not appear that Mr. Williams contends, that Congress is without power to authorize national banks to pay interest on deposits. It is conceded by him that this has been and can be done. The right is expressly given in Section 24 of the Federal Reserve Act, which, in terms referring to national banks, provides that -

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"such banks may continue hereafter as heretofore to receive time deposits and to pay interest on the same".

Section 19 provides in part that -

"Demand deposits within the meaning of this Act shall comprise all deposits payable within thirty days, and time deposits shall comprise all deposits payable after thirty days, and all savings accounts and certificates of deposits which are subject to not less than thirty days' notice before payment.

Inasmuch as Congress has the right to authorize the payment of interest on deposits as an incident to the business of banking and has exercised this right, the question arises whether or not a state law prohibiting banking associations not organized as Savings Banks under the laws of that State from advertising that it will receive savings accounts, can be held to prevent national banks from publishing such advertisement and from soliciting such accounts.

It is true, as stated by Mr Williams, that in the original House bill provision was made for the creation of separate savings departments and that this provision was eliminated by the Senate and agreed to by the conferees. In its stead the provisions above quoted, authorizing banks to pay interest on deposits and including savings accounts in the interest-bearing deposits, were incorporated. The question, therefore, of whether or not the State of California has the right to prohibit national banks from soliciting savings accounts would seem to depend upon whether such prohibition can be said to be an exercise of police power by the State and whether it is necessary for the protection of property within its limits.

The limitation of State legislation passed in the exercise of police power is fully discussed in the case of Railroad Co. v. Husen, 95, U. S., 470, where the Court says -

"We are thus brought to the question whether the Missouri statute is a lawful exercise of the police power of the State. We admit that the deposit in Congress of the power to regulate foreign commerce among the States was not a surrender of that which may properly be denominated police power. What that power is, it is difficult to define with sharp precision. It is generally said to extend to making

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regulations promotive of domestic order, morals, health, and safety. As was said in Thorp v. The Rutland & Burlington Railroad Co., 27 Vt. 149, 'it extends to the protection of the lives, limbs, health, comfort, and quiet of all persons, and the protection of all property within the State. *** ' ***

"But whatever may be the nature and reach of the police power of a State, it cannot be exercised over a subject confided exclusively to Congress by the Federal Constitution. It cannot invade the domain of the national government."

In the later case of Reid v. Colorado, 187, U. S., 137-147, the question is also considered in detail. The Court in that case, in discussing the right of the State of Colorado to enforce certain laws which were passed in the exercise of the police power of the State, says -

"It is quite true, as urged on behalf of the defendant, that the transportation of live stock from State to State is a branch of interstate commerce and that any specified rule or regulation in respect of such transportation, which Congress may lawfully prescribe or authorize and which may properly be deemed a regulation of such commerce, is paramount throughout the Union. So that when the entire subject of the transporation of live stock from one State to another is taken under direct national supervision and a system devised by which diseased stock may be excluded from interstate commerce, all local or State regulations in respect of such matters and covering the same ground will cease to have any force, whether formally abrogated or not; and such rules and regulations as Congress may lawfully prescribe or authorize will alone control. Gibbons v. Ogden, 9 Wheat. 1,210; Morgan v. Louisiana, 118 U. S. 455,464; Hennington v. Georgia, 163 U. S. 299,317; N. Y., N. H. & H. R. R. Co. v. New York, 165 U. S. 628,631; Missouri, Kansas & Texas Railway Co. v. Haber, 169, U. S. 613,626; Rasmussen v. Idaho, 181 U. S. 198,200. The power which the States might thus exercise may in this way be suspended until national control is abandoned and the subject be thereby left under the police power of the States.

Inasmuch, therefore, as Congress has the right to authorize national banks to charge interest on acounts and to include in such accounts what are generally known as "savings accounts", and since it has exercised this right, it would seem that the California statute referred to can not properly be so construed as to defeat this right.

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C. S. H. No. 4.

I cannot agree with Mr. Williams that depositors would necessarily be led to assume that savings acounts received by national banks would be subject to investment according to State laws, and while national banks should not be permitted to advertise themselves as "savings banks", since they are not so designated in the Act, power is specifically granted to member banks to receive interest-bearing accounts, including "savings accounts", and since they possess this power, the right to advertise for such accounts would seem to be a necessary incident to its exercise.

It is not believed, therefore, that the penalties prescribed by Section 49 of the Bank Act of the State of California could be legally enforced against a national bank which advertises that it will receive and pay interest on savings accounts.

Respectfully,

(Signed) M. C. ELLIOTT,

Counsel,

Honorable C. S. Hamlin,
Governor.

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FEDERAL RESERVE BOARD

WASHINGTON

February 23, 1915.

My dear Governor:

The attached letter from Governor McDougal raises the question whether drafts "payable on arrival of car" are eligible for rediscount by Federal reserve banks.

Section 13 of the Federal Reserve Act provides that any Federal reserve bank may discount "notes, drafts, and bills of exchange arising out of actual commercial transactions", and though this language does not in express terms demand that the paper be negotiable, it must be so construed, because of the whole spirit and purpose of the Act.

The Act evidently contemplates that title to eligible paper must pass with it and that in event of nonpayment a Federal reserve bank must be able to sue in its own name on such paper. To secure these rights the paper must be negotiable, otherwise the transfer would constitute a mere assignment and the holder would have to sue in the name of the payee. It must also be noted that if the paper is not negotiable a Federal reserve bank rediscounting it would hold it subject to the equities existing between the original parties to the bill. The same limitations would be imposed on the Federal reserve agent holding such paper as security for Federal reserve notes. The natural construction of the Act, therefore, is that paper must be negotiable in order to be eligible for rediscount.

The question presented in Governor McDougal's letter is whether a draft "payable on arrival of car" is negotiable. A draft to be negotiable must be an unconditional order to pay to the bearer or order a definite sum of money on demand or at a determinable future time. The drafts referred to above do not seem to comply with these conditions. Should the car fail to arrive, for any cause whatever, the draft would not be payable. The event or contingency upon which payment depends must be one which must necessarily happen in the natural course of the laws of nature. Weidler & Carpenter v. Kauffman, 14 Ohio, 455.

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The Negotiable Instruments Law, Section 4, which is based on settled decisions provides that:

> "An instrument is payable at a determinable future time, within the meaning of this Act, which is expressed to be payable
> (3) On or at a fixed period after the occurrence of a specific event, which is certain to happen, though the time of happening be uncertain."

In the case of Colehan v. Cooke, Willes 393, a note payable ten days after the death of the maker's father was held good on the ground that the father must die at some time and payment, therefore, was not dependent on the happening of an event which might fail to occur. But in the case under consideration, - that is, drafts "payable on arrival of car", there is no certainty whatever that the car will arrive, and such paper would probably be held to be non-negotiable on two grounds: first, that it is not an unconditional promise to pay; and second, that the time of payment is not fixed and certain because of the fact that the event by which it is determinable need not necessarily ever occur.

In all the cases on this point, there seems to be only one exception to this general rule that the note or bill must be payable at all events. That case is an English one decided some time ago - Andrews v. Franklin, 1, Strange, 24. A note payable two months after a certain ship was paid off was held negotiable even though the event was not necessarily bound to occur. The court in this case, however, admitted that paying off the ship was a contingency which would ordinarily make the note non-negeotiable, but went on to explain that because this ship was a government one, the payment was a government obligation which must be performed. But even on this ground, the case has always been discredited by courts in which it has been cited.

It seems quite clear, therefore, that a note or draft "payable on arrival of car", which may or may not arrive, would very probably be held non-negotiable, both at common law and under the Negotiable Instruments Law.

Respectfully,

(Signed) M. C. ELLIOTT,

Counsel.

Honorable C.S. Hamlin,
Governor.

2/26/15/

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FEDERAL RESERVE BOARD

WASHINGTON

February 13, 1915.

My dear Governor:-

The attached letter from Governor Strong raises a question as to the effect of waiver of demand, notice and protest upon the obligation of an acceptor of a domestic draft or bill of exchange discounted by a member bank under the provisions of Section 13 of the Federal Reserve Act.

An acceptor of a draft or bill is the party primarily liable, and the drawer and endorsers are merely sureties. 4 Am. & Eng. Encl., 470, 2nd Ed., and cases cited. In other words, his liability is the same as that of the maker of a note. He is the principal and not a collateral debtor. Blair v. Bank of Tennessee, 11 Humph. (Tenn.) 88.

The requirement that the holder make demand on the acceptor at maturity and give notice of dishonor is provided for the benefit of persons secondarily liable, such as the drawer or endorser, and is intended to protect such secondary party from the risk of loss which may occur because of delay in demanding payment from the party primarily liable or because of the fact that he has no notice that his principal has failed to pay. Stanley v. McElrath, 86 Calif. Rep., 457.

In other words, the law provides that the holder must demand payment at maturity and that in case the bill is not paid by the acceptor on demand, other parties subsequently liable must be given notice, in order that they may take any necessary steps to protect themselves. If they are not notified of demand and dishonor, they are entitled, as sureties, to conclude that the bill has been paid and that they are released. The acceptor, or primary debtor, on the other hand, is not entitled to notice, and, unlike the drawer or endorser, is not released on failure of presentment and demand at maturity. Daniel on Negotiable Instruments, 4th Ed., Vol. 2, P. 52; Hayes v. Northwestern Bank of Virginia, 9 Gratt, (Va.) 127.

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The right of other parties than the acceptor to receive notice is a personal one, and if it is not desired, may be waived, but such waiver can in no way affect any one other than the person making it. Such person merely surrenders a right afforded him by the law for his own protection.

It seems, therefore, that a waiver of demand, notice and protest on a bill discounted by a member bank under the provisions of Section 13 can have no effect on the acceptor of such bill. He remains liable just as though the formality due the person making the waiver had been complied with.

Respectfully,

(Signed) M. C. ELLIOTT,

Counsel.

Hon. Charles S. Hamlin,
Governor.

2/26/15/

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

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SUBJECT: Review of determination of Organization Committee, modification of districts created and change in designation of Federal Reserve Cities.

My dear Governor:-

I have the honor to acknowledge receipt of a copy of the resolution of the Board requesting an opinion on the following questions:

I. What are the general powers and duties of the Federal Reserve Board in reviewing the determination of the Organization Committee?

II. Can the Federal Reserve Board, under the terms of the Federal Reserve Act, designate other Federal reserve cities in place of those selected by the Organization Committee?

III. Can the Federal Reserve Board alter the geographical limits of the districts created by the Organization Committee?

IV. Can the Federal Reserve Board, by the consolidation of two or more districts, reduce the number of Federal reserve districts?

The provisions of the Federal Reserve Act which it is necessary to construe in considering the foregoing questions are contained in Section 2 of the Act and are as follows:

(a) "The determination of said organization committee shall not be subject to review except by the Federal Reserve Board when organized: Provided, That the districts shall be apportioned with due regard to the convenience and customary course of business."

(b) "The districts thus created may be readjusted", and

(c) "New districts may from time to time be created by the Federal Reserve Board, not to exceed twelve in all".

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A discussion of the general powers of the Board to review the determination of the Organization Committee necessarily involves a consideration of the other questions submitted, but as far as possible the several questions will be discussed separately in the order above indicated.

I. What are the general powers and duties of the Federal Reserve Board in reviewing the determination of the Organization Committee?

The scope of the power of the Federal Reserve Board to review the determination of the Organization Committee will depend very largely upon the construction to be placed upon the language "subject to review".

It is necessary to determine from the context, and from a general consideration of the circumstances under which the Act was passed, whether Congress intended (a) to vest in the Board the power to consider de novo the whole subject of determining Federal reserve districts and designating Federal reserve cities without reference to the decision of the Organization Committee, or (b) to vest in the Board the right to review the determination of the Committee in the same manner and to the same extent that an appellate court reviews a decision of the lower court.

If the former view is adopted it is necessary to conclude that Congress intended to vest no independent powers in the Organization Committee but to limit its functions to collecting and analyzing information to be submitted to the Federal Reserve Board for its consideration in designating the Federal reserve cities and in defining the geographical limits of the districts to be served. In other words, if no weight is to be given to the decision of the Committee and the Board is to consider the whole subject anew with reference to the determination of the Committee and without restriction, the work of the Committee is necessarily of no effect.

In view of the general character of the language used in vesting this power of review in the Board, and of the absence of any details as to the method of procedure to be followed, it is important to analyze the powers apparently vested in the Organization Committee and those vested in the Federal Reserve Board in order to determine what weight should be given to the decision of the Committee and to what extent and under what circumstances it is subject to modification by the Federal Reserve Board.

Powers of the Organization Committee.

From an examination of the Act it appears that, briefly summarized, the Organization Committee is empowered

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and directed -

(a) To designate not less than eight nor more than twelve cities to be known as Federal reserve cities.

(b) To divide the continental United States, exclusive of Alaska, into districts, each district to contain only one of such Federal reserve cities, and

(c) to supervise the organization in each of the cities so designated of a Federal reserve bank.

In performing these duties, the Organization Committee is authorized -

"To employ counsel and expert aid, to take testimony, to send for persons and papers, to administer oaths, and to make such investigation as may be deemed necessary by the said committee in determining the reserve districts and in designating the cities within such districts where such Federal reserve banks shall be severally located."

Powers of the Federal Reserve Board.

The Federal Reserve Board is empowered, in so far as the organization of the several Federal reserve banks is concerned -

(a) To appoint three of the nine directors of each bank and to designate one as the Federal reserve agent and chairman, and one as deputy Federal reserve agent, the three directors so appointed to be known as Class "C" directors.

(b) To call for payment of the first installment of subscription of the member banks.

This last power is vested alternatively in the Organization Committee and the Federal Reserve Board, and while the Organization Committee is not empowered to appoint the Class "C" directors, it is authorized to act as chairman of the Board of Directors (pending the appointment of such chairman by the Federal Reserve Board), in holding the election of the three Class "A" and three Class "B" directors of each bank. The remaining powers of the Federal Reserve Board, with the exception of certain duties in reference to the transfer of public stock, relate to the supervision of the Federal reserve banks when organized rather than to their organization.

It was clearly contemplated by Congress, therefore, that the organization of the several Federal reserve banks should be proceeded with immediately upon the passage of the Act, and that such organization might be carried to practical completion before the Federal Reserve Board, under the terms of the Act, should be called upon to exercise

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any specific powers in reference thereto. This is indicated not only by an analysis of the Act as it passed but also by the history of the particular provisions of the Act under consideration, as shown by the language in the House bill, the modifications made by the Senate, and the language agreed to by the Conference Committee.

It seems clear, therefore, that Congress expected that the right of review might be exercised by the Federal Reserve Board after, as well as before, the establishment of the Federal reserve banks. Consequently it must be assumed that the power to review the determination of the Committee is the same in either case.

The Act in terms vests a broad discretion in the Organization Committee, and the power to employ expert aid, to take testimony, to send for witnesses, etc., is vested exclusively in that Committee. Furthermore, it is required, under the provisions of the Act, after completing the work of designating the cities and determining the districts, to proceed immediately with the organization of the banks.

The conclusion appears to be fully justified, therefore, that Congress did not intend that the Committee should merely collect and analyze information for submission to the Board since otherwise it would have provided that the incorporation and organization of the Federal Reserve banks should be undertaken only after the Federal Reserve Board had rendered its decision and had thus given a more definitely fixed status to the districts created and the cities designated.

On the other hand, Congress manifestly intended to vest very broad powers in the Federal Reserve Board and inasmuch as the Board is charged with the supervision of the banks when created, and the responsibility of the successful operation of the system is so largely entrusted to its care, it seems clear that the decision of the Committee was not intended to be final but that the Board should have the right to modify the districts - (a) if, upon an examination of the record consisting of evidence submitted to and information collected by the Organization Committee, the Board should conclude that the districts are not apportioned with due regard to the convenience and customary course of business, or (b) if, as a result of the operation of the system, experience should demonstrate the fact that some other apportionment will best accomplish the purposes and objects of the Act.

This view seems entirely consistent with the alternative construction suggested, namely, that the right of review vested in the Board is analagous to the right of an appellate court to review the decision of a lower court.

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It is true that a court will ordinarily review a decision of a lower court only in those cases where there have been errors of law, or in the case of some newly discovered evidence,- that is, new matter which has arisen since the decision of the lower court and not evidence which might have been offered before that decision was rendered.

The failure on the part of the Organization Committee, however, to comply with the proviso of Section 2, namely, "that the districts shall be apportioned with due regard to the convenience and customary course of business", would constitute an error of law and would justify a review and modification by the Board of its determination. Unless, however, the Board finds upon its examination of the record referred to that the Committee has clearly failed to comply with the proviso quoted and has not, in its opinion, apportioned the districts as prescribed by statute, the decision of the Committee would seem to be final so far as the present proceedings are concerned.

History of Provisions Relating to Organization of Banks.

The history of the provisions of the Act under consideration furnishes additional evidence of the basis of the foregoing conclusions. The House bill conferred no power on the Board to review the decision of the Organization Committee on its own motion but provided that upon the application of not less than ten member banks a district might be readjusted. This bill provided that the Committee should consist of the Secretary of the Treasury, the Secretary of Agriculture and the Comptroller of the Currency.

The Senate bill provided that the Committee should consist of the Secretary of the Treasury and two other members of the Federal Reserve Board. The determination of this Committee, under the terms of the Senate bill, was made subject to review by the Federal Reserve Board. The Conference Committee restored the provisions of the House bill relating to the personnel of the Committee and retained the provision that the decision of the Committee should be "subject to review" by the Federal Reserve Board. The language used in the conference report was adopted when the bill became a law.

The Senate and House bills and the Act as passed all provided that the organization of the banks shall be proceeded with immediately upon the passage of the Act, evidently intending that the work of the Organization Committee should be acted upon at once and that it should not be subject to review except by the Federal Reserve Board, and then only for the reasons already stated.

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II. Can the Federal Reserve Board, under the terms of the Federal Reserve Act, designate other Federal reserve cities in place of those selected by the Organization Committee?

The power to designate other reserve cities in the place of those selected by the Organization Committee is not expressly given by the Act. In the bill as it passed the House, the Organization Committee was required to designate from the reserve cities authorized by law not less than twelve to be known as Federal reserve cities, and to divide the continental United States into Federal reserve districts. In the Senate bill the qualification that such cities should be selected from the reserve cities was removed and the selection was made entirely a matter of discretion with the Committee. The bill as it became a law left the designation of the cities a matter of discretion.

The qualification above quoted, limiting the discretion of the Organization Committee, and which provides that "the districts shall be apportioned with due regard to the convenience and customary course of business", refers specifically to districts and not to the cities designated. The Organization Committee is authorized -

> "to make such investigation as may be deemed necessary by the said Committee in determining the reserve districts and in designating the cities within such districts".

In defining the power of review vested in the Federal Reserve Board, the language used is -

> "The determination of said Organization Committee shall not be subject to review except by the Federal Reserve Board".

It appears, therefore, that the only limitation on the discretion of the Committee relates to the determination of the districts, and that the power of review likewise refers to that determination and does not refer specifically to the designation of the cities.

The power, therefore, to change the location of the Federal reserve banks is clearly not an expressed power under the terms of the Act and, if it exists, must be said to be implied -

(a) From the fact that construing the language "subject to review" in a broad sense, it may be said that to apportion the districts "with due regard to the convenience and customary course of business", it is necessary to consider the location of the Federal reserve cities in each district, notwithstanding the facts that the designation of cities appears to be a matter of discretion, and that this qualification refers to districts rather than to cities.

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or such power may be implied -

(b) From the fact that the power to "readjust" the districts created carries with it the power of designation of the Federal reserve cities, since a district may be so readjusted as to transfer a Federal reserve city to another district or as to place a Federal reserve city in an unsuitable portion of an altered district. In either case it would be necessary to designate a suitable Federal reserve city for the readjusted district.

If, therefore, the Board concludes that the districts are not apportioned according to the purpose and intent of the Act and determines that it is necessary to readjust such districts, it would seem clear that it possesses an implied power to change the designation of the Federal reserve cities. If, however, the districts are not readjusted, it seems very doubtful whether this power can be implied, and to change the designation of cities without readjusting the districts would necessitate resolving this doubt in favor of the exercise of this power against the apparent intent of Congress.

III. Can the Federal Reserve Board alter the geographical limits of the districts created by the Organization Committee?

The power to "readjust" districts, as shown above, is vested in the Board independently of the power to "review" the determination of the Organization Committee. The power to "review", as any court review, contemplates a review within a reasonable time, either before or soon after the establishment of the system, and, like a review by a court, should be limited to the evidence submitted to the Organization Committee, as suggested in the answer to Question I. The power to readjust, however, is not limited in time and would seem to be a continuing power, Congress evidently intending to provide a means for altering the districts even after the determination of the committee as such had become fixed by a lapse of time or by being affirmed by the Board.

Therefore, if, later, in the supervision of the actual operation of the several banks, it should be demonstrated that a readjustment of the geographical limits of the districts will best serve the purposes of the Act, the Board is expressly authorized to make such readjustment just as it can do so now under the power of review if, from the evidence submitted to the Organization Committee, it feels that the requirements of the Act were not complied with by that Committee.

IV. Can the Federal Reserve Board, by the consolidation of two or more districts, reduce the number of Federal reserve districts?

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I am unable to find in the Act any power, either expressed or implied, by which the Board can, by consolidation reduce the number of districts. It is true that it has the power to readjust the districts created but the power to "readjust" can hardly be said to include the power to eliminate, and any change which results in the elimination of a whole district could hardly be said to have been contemplated by the Act.

If Congress had intended the power to "readjust" to be sufficiently broad to authorize an increase or a reduction in the number of districts it would have been unnecessary to grant the express power refereed to above to create from time to time new districts not to exceed twelve in all. In other words, under the well settled doctrine of "expressio unius est exclusio alterius" the fact that Congress expressly granted the power to increase the number of districts but did not in terms grant the power to reduce the number indicates very clearly that it did not intend to vest this authority in the Board.

REGULATION NO. 1.

In view of the foregoing opinion, it seems proper to refer to Regulation No. 1 adopted by the Board, prescribing method of procedure in appeals from the decision of the Reserve Bank Organization Committee.

As above shown, the provision of the House Bill vesting in the member banks the right to file an application for readjustment of districts, was not incorporated in the bill as finally passed, but the matter of review and readjustment was left to the Board to consider on its own motion. In order that the Board might have the assistance of the views of the parties in interest, however, Regulation No. 1 was adopted and representatives selected by the parties interested were invited to discuss any questions of law or fact including the powers and jurisdiction of the Board.

In the discussion before the Board, the questions considered above were not argued at length. The jurisdiction of the Board to review the decision has not been questioned but Counsel for the Reserve banks have, in their arguments, taken the position that the decision of the Committee should stand unless clearly shown not to be in accordance with the purpose and intent of the Act, and have directed their arguments mainly to the merits of the case as disclosed by the record.

Respectfully,

(Signed) M. C. ELLIOTT

Counsel

Honorable Charles S. Hamlin,

Governor

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FEDERAL RESERVE BOARD

WASHINGTON

March 1, 1915.

SUBJECT: Interpretation of the language "based on the importation or exportation of goods" as used in Section 13 of the Federal Reserve Act.

My dear Governor:-

I have been asked for an opinion on the proper interpretation of that part of Section 13 of the Federal Reserve Act which reads: "Any Federal reserve bank may discount acceptances which are based on the importation or exportation of goods", with a view to determining whether the words "importation or exportation of goods " include (1) shipments between countries other than the United States, and (2) shipments between the continental United States and possessions of the United States.

Rules of Construction.

The first principles of statutory construction require that language which is clear and unambiguous be given its ordinary and natural significance. The legislative meaning is first to be sought in the words used and if they are clear, the letter of the law controls, unless in extraordinary cases such a natural construction would result in an obvious or absurd error. United States v. Goldenberg, 168 U. S. 95,102; United States v. Union Pacific Railroad Co., 91 U. S. 72,79; Lake County v. Rollins, 130 U. S. 662. "The legislature must be presumed to use words in the known and ordinary signification, unless that sense be repelled by the context", Levy v. McCartee, 6 Peters, 102,110. In Martin v. Hunter, 1 Wheat. 304,326, it is said that "where a power is expressly given, in general terms, it is not to be restrained to particular cases, unless that construction grow out of the context, expressly, or by necessary implication. The words are to be taken in their natural and obvious sense, and not in a sense unreasonably restricted or enlarged".

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In accordance with the decisions in these and other cases, unless such a result is absurd or obviously contrary to the intent of Congress as shown by other parts of the Act, the natural and usual significance must be attached to the words "importation" and "exportation". The question, therefore arises, what is their ordinary and popular meaning ?

In discussing this subject the co-relative terms, "export", "exportation","import", "importation", and the like will be treated as synonymous.

General Definition.

The Century Dictionary and Cyclopedia defines "export" as, "That which is exported, a commodity carried from one place or country to another", and "exportation" as, "The act of conveying or sending to a distance, especially to another state or country commodities in the course of commerce". The same authority defines "exporter" as, "One who ships goods, wares and merchandise of any kind to a foreign country or distant place for sale". The New Standard Dictionary defines "export" as, "That which is exported: in general, goods or any article of trade or merchandise sent from one country to another : properly, as used in the United States Constitution, goods sent to a foreign country".

If these broad definitions are applied, it is manifest that the words "importation" and"exportation" will include shipments between countries other than the United States. It therefore becomes necessary to determine whether these terms have become limited in their significance by judicial construction in those cases where the courts have been called upon to interpret this language as used in the Federal Constitution and in the several Acts of Congress.

Judicial Construction of Language as used in Federal Constitution and Statutes .

The word "import" as used in tariff statutes of the United States invariably refers to imports to the United States from a foreign country, and it might be argued that when the words "exportation" and "importation" are used in the Federal Reserve Act they must be given a corresponding significance - that is, they must be held to refer to exports from and imports into the United States from a foreign country.

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This argument, however, is not convincing, because of the fact that the word "import" as used in tariff laws must necessarily refer to shipments into the United States. "The power of Congress to levy and collect taxes, duties and excises is co-extensive with the United States", Loughborough v. Blake, 5 Wheat. 317. To levy a duty or tax of any sort, a sovereign must have jurisdiction over the article taxed. This narrower construction of the word "import" was, therefore, necessary, in order to give the tariff laws any effective operation. The United States could have no possible jurisdiction over a transaction between Buenos Aires and London, for instance, and to attempt to tax such an import would be ineffectual.

But even in these tariff laws where the meaning of "import" must necessarily be limited to imports into the United States, Congress has almost invariably provided in terms that the imports be from a foreign country into the United States. In the first tariff act, passed by Congress on July 4, 1789, it was enacted - "That *** duties *** be levied on the following goods, wares and merchandise imported into the United States from any foreign port or place", and it is to be noted that practically every tariff law passed by Congress since that time has contained some similar provision.

It might be contended that this restriction limiting dutiable imports to articles brought from a foreign country to the United States was intended to preclude any consideration of articles imported into one State from another State of the Union. But such intention is rebutted by the fact that the Constitution as construed by the Supreme Court of the United States, does not give Congress the power to lay an impost on goods imported from another State. The Constitution gives to Congress the general power "to levy and collect taxes, duties, imposts, and excises", but "imposts" has been construed in Woodruff v. Parham, 8 Wall. 123, to mean a duty, custom, or tax levied on articles brought into the United States, and the words "imports" and "exports" as used in the Constitution, are uniformly held to refer only to goods imported from foreign countries into the United States, and not to articles carried from one State to another. Pittsburgh Coal Co. v. Louisiana, 156, U. S. 590, 600; Brown v. Houston, 114 U. S. 622, 628.

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It seems clear, therefore, that "import" or "export" as used in Federal tariff statutes must of necessity refer to transactions to or from the United States.

Federal Reserve Act and Other Federal Statutes Distinguished.

On the other hand, in the Federal Reserve Act - which is not a tariff measure, but which is, on the contrary, a law in which the words "importation" and "exportation" could consistently refer to transactions between two foreign countries other than the United States, - Congress has failed to put any restrictive limitation, evidently intending that the words used be given their normal and natural significance, the meaning generally understood when used in ordinary commercial parlance. The lexicons all agree in defining "export" as an article or commodity carried from one country to another, and nowhere except in cases construing the Constitution and the tariff laws is there any suggestion that "import" necessarily means an article shipped from a foreign country to the country or jurisdiction of the person or legislature using the word.

When used in the Federal Constitution or in the tariff laws made in pursuance thereof, the words "import" and "export" must necessarily be given the narrower construction, for the reason already stated - that is, the United States has no jurisdiction to impose a tax or impost on any article not within the confines of the United States. But in the case of a Federal banking law, where there is nothing in the context nor in the spirit of the Act to demand a narrower or limited interpretation, the words should be given their full significance. All the cases previously cited on the laws of statutory construction demand this result.

Significance as used in Federal Reserve Act.

But even if the literal meaning of the phrase "importation or exportation" be considered doubtful, a liberal construction in accordance with the general intent of Congress would necessitate this same result. It must be remembered that the Federal Reserve Act is remedial and constructive legislation by which Congress clearly intended to eliminate certain patent evils in conditions as they existed at the time of enactment, and to establish on a broad, comprehensive, and firm basis a unifying system of banking. The language "to

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furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes", contained in the title of the Act, shows that it is remedial, and as such should be broadly and liberally construed in order to accomplish the advancement of the remedies contemplated. 24 Am. and Eng. Encl. 887, and cases cited.

It may be reasonably assumed that Congress not only wanted to create a discount market for acceptances, but at the same time intended to establish a system which would facilitate the trade and commerce of the people of the United States, no matter where that trade or commerce originated or what its destination. Acceptances having become a recognized incident of trade, as between nations the establishment of a wider market in this country for such paper was apparently one of the objects of the Act.

Both the Senate bill and the conference agreement permitted the discount of acceptances, based not only on foreign but also on domestic shipments. The latter, however, were struck out on the floor, probably because of the fear that a general domestic acceptance business might be abused by the smaller banks which were unfamiliar with this class of investment and that for the present at least, such investments might prove a detriment not only to such banks but to the entire system. The elimination, however, of acceptances based on domestic shipments could not have been intended to restrict or limit the field of acceptances based on the "importation or exportation of goods", that phrase remaining precisely the same as it was prior to the elimination of domestic acceptances and just as it read when the intent was to include acceptances based on shipments of any kind.

It seems, therefore, that by all the ordinary rules of statutory construction, giving to the words the natural and ordinary import, which is strongly corroborated by the purposes, spirit and history of the Act, this portion of Section 13 was intended to, and actually does, permit the discount of acceptances based on the importation and exportation of goods, not only to and from the United States, but also as between other countries, separate and apart therefrom.

Shipments to and from Island Possessions of the United States.

The second question raised is whether the clause "acceptances which are based on the importation or exportation of goods", should include acceptances based on shipments between the continental United States and its possessions; viz., Porto Rico, Hawaii, Canal Zone and the Philippines.

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It is, of course, not to be disputed that if, as contended above, imports and exports to and from countries other than the United States are a satisfactory basis for acceptances, then acceptances based on shipments between any of these possessions and another country, other than the United States are eligible, a fortiori.

This leaves to be considered the one question just stated.

The definitions given in the standard dictionaries refer to shipments from one country to another country or to a "distant place", and such a general understanding of the words in question would certainly seem to be sufficiently comprehensive to include transactions between the United States and any of its island possessions, though they are not foreign territory in a political sense.

To permit the discount of acceptances based on the importation or exportation of goods from and to the possessions of the United States, it must be shown (1) that these words, as generally known and understood and as intended by the Federal Reserve Act, do not necessarily refer to shipments to and from a foreign country, and (2) that shipments to and from these possessions are not domestic shipments.

As already shown, the word "import" as used in the Constitution and tariff laws, has been construed by the Supreme Court to refer to imports from foreign countries. In the tariff laws this has necessarily been so because these laws specifically require that the import be from a foreign country. The words as used in the Constitution, however, not being expressly limited, has been construed to refer to imports from a foreign country and not to articles shipped from one state to another, for various reasons. A study of the discussions in the Constitutional Conventions and of the history of the formation of the Constitution showed that there was no intention in the minds of the framers of that instrument to refer to anything but foreign imports and exports, and the Supreme Court has, in various decisions reciting the history and development of the Constitution and the evils to be obviated by it, decided that "export" and "import" mean exports and imports to and from foreign countries and not between states. But in all those cases the particular circumstances under which the words were

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used were stated at length to show why this narrower interpretation was necessary in each instance. Woodruff V.Parham 8 Wall. 123; Brown V. Houston, 114 U. S. 622. In other words the burden of limiting the natural meaning of the words was clearly recognized by the Court. Justice Brown in referring to this well-settled construction of the words as used in the Constitution, said, in Dooley V. United States, 183 U. S. 151, 153, -

> "While the words 'import' and 'export' are sometimes used to denote goods passing from one State to another, the word 'import', in connection with the provision of the Constitution that 'no State shall levy any imposts or duties on imports or exports', was held in Woodruff V. Parham, 8 Wall.123, to apply only to articles imported from foreign countries into the United States".

thus implying that they are used in other than the Constitutional sense. But as previously explained, there is no necessity for forcing a restricted construction on this phrase as used in the Federal Reserve Act, and in consequence there would seem to be no justification for reading the word "foreign" into its definition as applied to this Act.

It might be contended that to follow out this argument logically would lead to the conclusion that a shipment of goods from one state of the United States to another state of the United States would be an "importation or exportation of goods",a result clearly not contemplated by Congress. The answer is found in the history and development of the Act before its passage.

The House bill provided for the discount of acceptances based on the "exportation or importation of goods". The Senate bill amended this provision to read "importation or exportation or domestic shipment of goods", evidently intending to cover shipments to and from any points wherever located. As the Act read when finally passed, "domestic shipments" were eliminated. It is evident, therefore, that Congress intended to make eligible acceptances based on all except domestic shipment of goods.

Status of Insular Possessions.

This raises the second point : Is a shipment from the continental United States to one of the island possessions of the United States a domestic shipment ? The Century Dictionary and Cyclopedia defines "domestic commerce" as, " commercial

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transactions within the limits of one nation or state", and in 14 Cyc. 829, quoting In re Roofing Contractors Association, 9 Pa. Dist. 569, 570, domestic trade is referred to as, "the exchange or buying or selling of goods within a country". But the difficulty is that the term "United States" has various different meanings dependent upon whether it is used in a geographical, commercial or governmental sense, or whether it is intended to describe the States of the Union as such.

The term "United States" as used in the uniformity clause of the Constitution has been held in the Insular cases not to extend to the unorganized territorial possessions of the United States. On the other hand, in dealing with foreign sovereignties, it is generally understood to have a broader meaning than when used in the Constitution. It then includes all territories subject to the jurisdiction of the Federal government, whether it is merely territory appurtenant to the United States, or whether it is an incorporated part of the United States.

This question of the status of our territorial possessions has been the subject of extended discussions before the Supreme Court and though it is now generally admitted that these possessions are not foreign in an international sense, nevertheless they may be foreign to the United States in a domestic sense. Downes v. Bidwell, 182 U. S. 244. In the case of Dorr v. United States, 195 U. S. 138, 143, the Supreme Court, in speaking of the extent and limitations of the Constitution as applied to our possessions said:

> "The limitations which are to be applied in any given case involving territorial government must depend upon the relation of the particular territory to the united States, concerning which Congress is exercising the power conferred by the Constitution. That the United States may have territory, which is not incorporated into the United States as a body politic, we think was recognized by the framers of the Constitution in enacting the article already considered, giving power over the territories, and is sanctioned by the opinions of the justices concurring in the judgment in Downes v. Bidwell, supra."

In other words, the United States may own territory which is subject to the control of Congress under the territorial

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clause of the Constitution, but which is not an integral part of the United States until Congress sees fit to make it such and to extend to it the operation of the Constitution and laws of the United States. The doctrine that the Constitution does not follow the flag, ipso facto, seems well settled now by numerous cases of the Supreme Court. See Downes v. Bidwell, supra; Hawaii v. Mankichi, 190 U. S. 197. It is, of course, admitted in all these cases that Congress may, if it chooses, incorporate into the Union any territories belonging to the United States. Until it does so, however, it seems, from the cases cited, that unorganized territories, though subject to the jurisdiction of Congress, are not domestic in a national sense, and that shipments to and from such territories are not to be considered domestic shipments within the meaning of the Federal Reserve Act.

It may be well to consider, separately and briefly, the cases of Porto Rico, the Philippines, Canal Zone, and Hawaii, to determine whether Congress has so acted as to make them an integral part of the United States.

PORTO RICO. Porto Rico is not foreign territory within the meaning of the Dingley Tariff Act, approved July 24, 1897, taxing articles imported into the United States from "foreign countries". DeLima v. Bidwell, 182 U. S. 1, decided May 27, 1901. In another case - Downes v. Bidwell - decided the same day, the Supreme Court held that the Foraker Act of April 12, 1900, which levied certain duties on articles coming into the United States from Porto Rico, and on goods shipped from the United States to Porto Rico, was valid, even though a tax or burden on shipments between different parts of the United States, is unconstitutional, because "Porto Rico is a territory appurtenant and belonging to the United States but not a part of the United States within the revenue clauses of the Constitution".

The duties in question are no longer levied, they were only a temporary assessment, but the status of Porto Rico remains the same, no Act of Congress having been passed to make it an integral part of the Union. Not being a part of the United States, and not being subject to the general laws of Congress unless specifically referred to in those laws, it cannot be contended that a shipment between Porto Rico and the United States is a domestic shipment in the generally accepted meaning of that term, a shipment from one part of the country to another.

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PHILIPPINE ISLANDS. In the case of Fourteen Diamond Rings v. United States, 183, U. S. 176, it was held that the Philippines are not a "foreign country" in the meaning of the Tariff Act of 1897, imposing a duty on imports from foreign countries. The court went on to say that "In this respect there is no distinction between the Philippines and the Islands of Porto Rico. Neither of them is a foreign country within the terms of that Act".

In the later case of Dorr v. United States, supra, it was held that the Philippines were not incorporated into the United States by the mere treaty of cession and as the court said:

> "The legislation upon the subject shows that not only has Congress hitherto refrained from incorporating the Philippines into the United States, but in the act of 1902, providing for temporary civil government, 32 Stat. 691, there is express provision that section eighteen hundred and ninety-one of the Revised Statutes of 1878 shall not apply to the Philippine Islands. This is the section giving force and effect to the Constitution and laws of the United States, not locally inapplicable, within all the organized territories, and every territory thereafter organized, as elsewhere within the United States".

The Philippines, like Porto Rico, are therefore not a part of the United States, and as Justice White said in Downes v. Bidwell, supra, "it is foreign to the United States in a domestic sense because not incorporated into the United States". Being generally understood to be foreign to the United States in every sense except an international one, there is no justification for the conclusion that shipments to and from the Philippines are domestic.

HAWAII. Though the Hawaiian Islands were not made an integral part of the United States by the mere Act of Congress annexing them, 30 Stat. 750, Hawaii v. Mankichi, supra, nevertheless by the Act of Congress of June 14, 1900, 31 Stat. 141, they were formally incorporated. By this Act the Constitution and all Federal laws were given "the same force and effect in Hawaii as elsewhere in the United States", and Justice White, in the case cited, said that by this Act "the islands were undoubtedly made a part of the United States in the fullest sense".

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This distinction between Hawaii and the Philippines and Porto Rico is recognized by all the branches of the Government. Porto Rico and the Philippines are under the jurisdiction of the Bureau of Insular Affairs in the War Department, but Hawaii is not. Hawaii, like Alaska, is represented in Congress by a territorial delegate, whereas the Philippines and Porto Rico merely send "resident commissioners" to Washington.

Under all the facts, therefore, Hawaii, must be considered as an integral part of the United States and practically and logically any shipment between Hawaii and the continental United States must be a domestic shipment. Congress having shown its intent to bar the discount of acceptances based on "domestic shipments", it would seem not possible to differentiate dealings with Hawaii from those with any part of the continental United States. Its relation to the United States seems precisely analagous to Alaska.

CANAL ZONE. The status of the Canal Zone is unique. The United States has, in effect, an easement ten miles wide across the Republic of Panama. It is foreign territory, subject to the control and supervision of this Government. The Tariff Act of 1913, imposing duties on imports "into the United States or into any of its possessions (except the Philippine Islands, and the islands of Guam and Tutuila)" does not apply to the Panama Canal, even though it is not expressly excepted from the term "possessions", as is the case with the Philippines. By an Act dated March 2, 1905, 33 Stat. 843, Congress specifically stated that "all laws affecting imports of articles, goods, wares and merchandise, and entry of persons into the United States from foreign countries, shall apply to articles, etc., coming from the Canal Zone and seeking entry into any State or Territory of the United States or the District of Columbia", showing that in no way is the Canal Zone considered an integral part of the United States. Indeed it is not even territory owned by the United States, but rather territory under its jurisdiction and control. Strictly speaking, it is a dependency. As such, it is far less a part of the United States than Porto Rico, and shipments to and from it could hardly be considered domestic shipments in the light of the previous discussion.

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To summarize: it would seem that the Federal Reserve banks may, under Section 13, discount acceptances based on the shipment of goods.

(a) between the United States and any foreign country.

(b) between any two or more foreign countries, and

(c) between the continental United States and Porto Rico, the Philippines or the Canal Zone.

but not acceptances based on the shipment of goods between the continental United States and Hawaii.

Respectfully,

Counsel.

Honorable C. S. Hamlin,
Governor.

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STATEMENT FOR THE PRESS.

March 4, 1915.

It was announced today at the offices of the Federal Reserve Board that the Board had determined to direct the introduction of a voluntary reciprocal plan of immediate clearance at all those Federal reserve banks where a clearing plan is not already in operation, the same to take effect with as little delay as possible. Letters are being sent to all Federal Reserve Agents and the latter are directed to take the matter up at once with their boards of directors.

The Federal Reserve Board does not prescribe details inasmuch as it has found in those districts where general clearing is already being practiced that the best results were obtained by leaving the control of such details in the hands of the local authorities. It, however, states that it will approve as a beginning a reciprocal arrangement whereby banks assenting to the plan will be given the privileges of immediate clearance at par upon all other banks similarly assenting.

It is the belief of the Board that within a short time a general clearing arrangement will be in operation in all districts and that this will be gradually extended so as to embrace the bulk of the banks in the system.

The plan does not provide for the settlement of the balances between Federal Reserve Banks or for the inter-district clearing of checks. It is an intra-district clearing plan pure and simple, the inter-district phases of the problem being reserved for future treatment.

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CONFIDENTIAL - For Members Only.

Circular No. __.
Series 1915.

FEDERAL RESERVE BOARD.

Washington, February 15, 1915.

Check Clearings.

Section Thirteen of the Federal Reserve Act provides in part:

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

The receiving on deposit of checks and drafts of other banks necessarily involves the collection of such items and since Federal reserve banks are authorized to accept (a) checks on their own member banks, (b) checks on other Federal reserve banks, and (c) when remitted by other Federal Reserve Banks checks on banks which are members of other Federal reserve banks, it will become necessary, when a general exchange business is undertaken, to deal with the problem of (1) intra-district clearing of checks, (2) adjustment of balances as between Federal reserve banks, and (3) inter-district clearing of checks.

The Board has determined that the purposes of the Act can be best attained with the minimum disturbance of existing conditions by providing, first for intra-district clearing; and when this phase of the problem has been properly disposed of the systematic adjustment of Federal reserve bank balances and inter-district clearings can be provided for as a natural and logical development.

Section Sixteen of the Federal Reserve Act imposes the obligation upon the Federal Reserve Board to prescribe charges to be made for the service of clearing checks when the Federal reserve banks undertake to exercise this power vested in them under Section Thirteen. In order that these charges may be based upon the results of actual experience and may not be merely estimated, the Board has determined, after due consideration, to recommend to the several Federal reserve banks the following plan of procedure as a means to this end:

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No. 2.

Reciprocal Privileges.

It is suggested that each Federal reserve bank offer to each of its members the reciprocal privilege of having all checks and drafts on other solvent member banks in its district entering into such agreement credited immediately to its account at par on the date of deposit, provided, such bank will authorize in writing the Federal reserve bank to charge to its account checks and drafts drawn on it and deposited by other member banks in its district, or by the United States Government. That to avoid depletion of reserve accounts each member bank availing itself of this reciprocal privilege shall agree to maintain on deposit with the Federal reserve bank a sum sufficient to protect, on a certain average, any net debit balance created by charging up checks and drafts drawn against it by other depositors.

In order to determine the sum necessary to be maintained in addition to its legal reserve, it is suggested that for the first sixty days after such arrangement goes into effect each bank entering into such arrangement shall maintain an additional sum equivalent to per cent of its legal reserve and after the expiration of sixty days shall maintain an additional sum on deposit equal to the average daily debit balance shown on its reserve account during that period.

After a canvass has been made by circular letter sent to all member banks, each Federal reserve bank should publish a list of those member banks which have agreed to the arrangement suggested and should thereafter agree to receive on deposit at par from all of such banks checks or drafts drawn against any banks shown on such list.

Whenever additional member banks agree to this arrangement the list should be revised so as to include in the par list all banks entering into this agreement.

Checks or drafts deposited by member banks not on the par list should be received for collection and deferred credit only and should not be credited to the depositing bank nor charged to the member banks against which such checks or drafts are drawn until the collection has been actually made.

Pending the establishment in the foregoing manner of a system of intra-district clearing, Federal reserve banks should not be required to handle checks on banks which are member banks of other Federal reserve banks and checks on one Federal reserve bank should not be received by other Federal reserve banks except for collection and credit.

As stated, the subject of adjustment of balances as between Federal reserve banks and inter-district clearing will be considered by the Board at a later date.

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Reports of Member Banks to Federal Reserve Banks and the Publication of a Summary by the Federal Reserve Board.

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For the purpose of ascertaining the general condition of member banks in each Federal reserve district, the Federal Reserve Board has decided to call for monthly report showing the condition of each member bank, which report is to be sent to the head office of the Federal reserve bank at the close of business on the last Friday of each month. Member banks located in reserve and central reserve cities will report twice monthly, at the close of business on the second and last Friday of each month.

The figures are to be compiled and telegraphed to the Federal Reserve Board. A brief summary of the condition of member banks in each Federal reserve district and a combined statement of all member banks will be published by the Federal Reserve Board not later than Saturday of the following week.

The report is not intended to show assets and liabilities in detail, as required by the periodical reports made to the Comptroller of the Currency, but rather to show the changes in the principal items, in the condition of member banks. In fact, it will serve three-fold purpose.

1. To keep the Federal reserve banks informed as to the cash and credit condition of member banks.

2. To keep Federal reserve banks informed as to encroachments upon reserve requirements.

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QUESTIONAIRE IN REGARD TO BRANCHES OF FEDERAL RESERVE BANKS.

1. What should the functions of a branch of a Federal Reserve Bank be? For example, should such a branch perform for certain specified member banks all the functions of the parent bank, or should it be restricted as to its functions?

2. Should certain territory be assigned to a branch bank or should member banks be authorized to deal voluntarily either with the parent or the branch?

3. Is there a real demand so far as you know for the creation of branches in your district, and if so to perform what functions?

4. How many Reserve Cities (if any) are there in your district which are more than fifteen hours' rail journey from your Reserve Bank?

5. By what percentage would your cost of operation be increased by the opening of one or more branches? What is the minimum force with which you could operate a branch?

6. Would any useful purpose be served by establishing, at cities upon or near the boundary line of other districts, joint or adjoining branches?

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Would it be Wise or Proper for Federal Reserve Board to Authorize Federal Reserve Banks to Pay their Member Banks, say One Percent, or Possibly Two Percent Interest on Deposits in Excess of Legal Requirements?

FIRST:

Except in Central Reserve Cities, only one-third of the reserve deposits have been paid in, and it will be six months before another instalment will come in and two and a half years before it is all paid in. Even in the end it is optional with the member banks whether they shall keep more than the required percentage of their reserves in their own vaults or in the vaults of the Federal Reserve Banks.

NOTE: At the end of 36 months the member banks will have the option of keeping the following percentages of their demand deposits in the manner indicated, depending upon their location:

	(a)	(b)	(c)	(d)	(e)
Member Banks Located In	Required Minimum In Own Vaults	Required Minimum Federal Reserve Bank Vaults	Reserve Which at Option of Member Bank may be Kept in Federal Reserve Bank or in Own Vaults	Total of (b) and (c)	Total Reserves
Central) Reserve) Cities)	6%	7%	5%	12%	18%
Reserve) Cities)	5%	6%	4%	10%	15%
Country) Cities) & Towns)	4%	5%	3%	8%	12%

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SECOND:

It is a recognized fact that cash reserves in the hands of the Federal reserve banks can be used expansively two and one-half times for one, whereas the same reserves in the vaults of the member banks have not that potentiality.

THIRD:

The temper of the American people does not brook delay. After a thing has been widely considered the people want results. The Federal reserve banks, while endeavoring to equip themselves for full operations, find themselves handicapped by the fact that for two and one-half years they must compete actively with the banks in Central reserve and reserve cities, which are permitted to hold reserve deposits of other national banks and at the same time are permitted to pay interest on those deposits. The Federal reserve banks must therefore either expect the member banks to make sacrifices in keeping excess reserves with the Federal reserve banks or must operate only in a limited way until the remaining reserves shall have been paid in.

FOURTH:

One of the principal and very natural reasons for opposition to the introduction of a general clearing plan is the fact that country banks may now collect their city items

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through their city correspondents and, while having this service rendered for them free, are given the benefit of counting as reserves the deposits in the hands of city correspondents and besides being given at least two percent interest on their balances. City correspondents are, in many cases, giving country banks the benefit of immediate credit on items received and deferred debit for items collected. In other words, the city correspondent is in many cases carrying the "float", besides giving the country bank interest on its deposits and at the same time acting as collection agency.

FIFTH:

It must be admitted that the immediate charge against member banks' reserve deposits of items even though endorsed by the depositing member banks, involves some risk to the Federal reserve bank, because the aggregate of items so charged, as experience has already shown, sometimes considerably exceed the reserve deposit of the bank against whom drawn. The risk on this account will, however, greatly diminish when the succeeding installments of reserve deposits have been made. The difficulty is that in the next six months the risk may be considerable. The question therefore arises, how can Federal reserve banks create an insurance fund by securing excess reserves

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from member banks in the face of the fact that national banks in Central reserve and reserve cities are able to offer inducements already referred to?

SIXTH:

It is likely that two or three of the Federal reserve banks will, in the next six months, be obliged to rediscount a considerable amount of commercial paper with other Federal reserve banks and will have to pay for this rediscounting privilege four percent or more. Might it not be better for the Federal reserve bank to exhaust the resources of its own District before going outside? In other words, might not the Bank of Atlanta more wisely pay one, or even two percent for balances of member banks in excess of legal reserves than to pay New York, Philadelphia or Chicago four percent?

It may be argued that these reserves will diminish the resources of the member banks, but it may be truly answered that it will not diminish those resources, for the reason that the reserves of member banks in the hands of the Federal reserve bank of the district will be more effective than if they remained in the vaults of the banks of Central reserve and reserve cities.

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SEVENTH:

It may be said - and in this the writer concurs - that the practice of paying interest on checking deposits is mischievous. It will be remembered that, in its original form, the Federal Reserve Act contemplated forbidding the payment of interest on active deposits, either by the Federal Reserve Bank or by member banks; but this provision was stricken out of the Act. Why, it may be inquired, should the Federal Reserve Board authorize the Federal Reserve Banks to initiate a practice which it considers vicious, simply because the law does not prohibit it or because it does not deny member banks the privilege? The answer is that the most effective way of stopping a practice of this kind by the member banks is by authorizing the Federal Reserve Banks to do it. When the Federal Reserve Banks have been put in position to meet the competition of the member banks in this practice their bonds have been greatly strengthened, and the chances are that at the end of two or three years the Board can look forward to the likelyhood of abolishing or greatly restricting this pernicious practice, although in saying this, it is admitted that the number of state banks remaining outside the system and the influence which they will have on the situation will have a very important bearing on the final outcome.

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EX-OFFICIO MEMBERS
WILLIAM G. McADOO
SECRETARY OF THE TREASURY
CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

184½ · 269

FEDERAL RESERVE BOARD

WASHINGTON

W. P. G. HARDING, GOVERNOR
PAUL M. WARBURG, VICE GOVERNOR
FREDERIC A. DELANO
ADOLPH C. MILLER
CHARLES S. HAMLIN

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

March 19, 1915.

S I R :

The Federal Reserve Board, shortly after it was organized, authorized the printing and engraving of two hundred and fifty millions of Federal Reserve notes. A few weeks ago it was decided, in view of the retirement of almost all of the "Aldrich-Vreeland"currency, to increase the stock on hand of Federal Reserve notes to five hundred millions, which is the amount of notes formerly kept on hand of "Aldrich-Vreeland" currency. The question has now arisen as to where this stock of notes should be kept on hand. Eight of the Federal Reserve Banks are near enough to Washington so that, with a stock of notes on hand in Washington, they could be supplied on comparatively short notice, say twenty-four to thirty-six hours at the outside. With respect to four of the banks, Minneapolis, Kansas City, Dallas and St. Louis, there is a more difficult problem.

A committee of the Board on Issue and Redemption has been studying this matter and reported in favor of keeping on

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hand a stock of 20 per cent of the total supply at the nearest subtreasury, a method which is authorized in the Federal Reserve Act, but some serious difficulties have developed in carrying out this plan.

Every time the notes change hands they have to be counted and a receipt taken; for if a receipt is taken for packages without counting the contents, it is of little or no value. The Comptroller of the Currency is not disposed to allow a large supply of notes to be kept for emergency purposes in various subtreasuries of the country with no check upon them and no receipt releasing him fully, because, under such a method, at some future time (it might be as much as five or ten years hence) it might be found that some sealed packages did not "tally up". By the same token the subtreasuries are undisposed to accept packages of money and give receipts therefor without counting their contents, especially if they are expected to carry this emergency supply an indefinite period, subject to call by the Federal Reserve Banks.

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Under all the circumstances the following plan is suggested for the consideration of the Federal Reserve Agents:

First: The appended table shows the total of notes which have been or are to be printed for each Federal Reserve Bank at present. It is proposed that the major part of this supply shall be held at Washington, subject to call, but it is thought, especially in the case of the more distant banks, that an emergency supply near at hand is desirable.

The Committee on Issue and Redemption has felt that in the case of San Francisco a supply of 40 per cent should be kept on hand in San Francisco and in the case of some of the other reserve banks 20 per cent at the most should be kept. In the case of the banks near Washington the entire supply could be held at Washington.

Second: Where a bank considers that it should have a supply of notes for emergency purposes, it is suggested that some representative of the bank shall be appointed and sent to Washington to supervise the counting of the notes in

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Washington. This representative, after each package of notes is made up, shall affix his seal to the package in addition to the seal of the Comptroller's office. It is proposed that this counting shall be done at the Bureau of Engraving and Printing by employees of the Bureau of Engraving and Printing (or else at the Comptroller's office) under the supervision of the Division of Issue of the Comptroller's office and the representative appointed by the Federal Reserve Bank.

In this connection, it might be desirable that the Federal Reserve Banks should unite in the selection of a joint representative.

Third: It is proposed that the Federal Reserve Banks desiring this emergency supply shall make their own arrangements for storage and safekeeping of this supply and have the notes shipped direct from the Bureau of Engraving and Printing in Washington to the place where the notes are to be kept, the idea being that this might be the subtreasury, or some other adequate and proper vault

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space. In the judgment of the Committee of the Federal Reserve Board these packages of money, under joint seal as above described, should be so safeguarded that they can be withdrawn only on the joint authority of two or three officers, of which the Federal Reserve Agent or the Deputy Federal Reserve Agent should be one and with the further safeguard of telegraphic authority of the Federal Reserve Board in Washington.

The above plans are submitted to you for your consideration and I shall be glad to hear from you at as early a date as possible.

Yours truly,

For the Committee of the Federal Reserve Board on Issue & Redemption.

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RESOLUTION OF THE FEDERAL RESERVE BOARD

Agreed to at a Meeting Held

Monday, March 22, 1915.

WHEREAS, The framers of the Federal Reserve Act had in contemplation the establishment of a co-ordinated system of banking in the United States under effective Governmental supervision, and

WHEREAS, It is the opinion of the Federal Reserve Board that the interests of the Government, the banks and the public will be best served, and the success of the system best assured by a membership which will include as many as possible of the banks made eligible under the terms of the Act, and

WHEREAS, In order to equalize the powers of the State and national banks as members of the system, the provisions of the Act extend to State banks and trust companies the privilege of membership, when not in contravention of State laws, and empower the Federal Reserve Board to extend the powers of national banks by granting such banks permission to act as trustee, executor, administrator, and registrar of stocks and bonds, when not in contravention of State laws, and

WHEREAS, It appears from an examination and analysis of the laws of the several States that banks created and organized under the laws of certain States cannot become members, and the right to exercise the powers of trustee, executor, administrator, etc., cannot be extended to national banks in certain States by reason of the laws of such States;

NOW, THEREFORE, BE IT RESOLVED, That the Federal Reserve Board is in entire sympathy and accord with the efforts of those who are advocating legislation designed to remove such restrictions and to make possible the perfection of a system of banking which will uniformly serve the interests of the public in all of the Federal reserve districts.

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Released for use Tuesday morning March 23, 1915.

STATEMENT FOR THE PRESS.

March 22, 1915.

The Federal Reserve Board has upon petition of banks in that vicinity, designated the City of Nashville, Tenn., as a reserve city.

The population of Nashville according to the census of 1910 was 110,364.

The action taken was recommended by the Federal Reserve Agent at Atlanta, Georgia.

The combined deposits of the six (6) National banks in Nashville is stated in the petition as $20,077,907.

The Board has adopted the following requirements as necessary before consideration will hereafter be given to the designation of any city as a reserve city:

> A population of at least 50,000; combined capital and surplus of national banks in the applying city of not less than $3,000,000, with deposits of not less than $10,000,000; endorsement of the application by at least fifty (50) national banks located outside of the applying city who will state that they are carrying or intend to carry upon such designation, accounts with a national bank in the applying city. Applications will be referred for report and recommendation to the Federal reserve bank of the district in which the applying city is located, whose chairman shall certify the names of the national banks endorsing the application.

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188 b.

Tentative Circular No___
Series 1915.

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FEDERAL RESERVE BOARD

Washington, D.C.May 6,1915.

A coordinated banking system, embracing in its membership State institutions as well as National banks, is the aim of the Federal Reserve System.

There can be but one American credit system of nation-wide extent, and it cannot attain its fullest potentialities if it rests upon an incomplete foundation, and fails to include the greater part of the strong and well managed banks of the country, whether large or small.

In the development of the new banking system, far-sighted and unselfish cooperation is expected of the banking community, and it seems clear that some basis can be found for harmonizing differences of interest or advantage existing among the National banks, State banks or trust companies, so far, at any rate, as may be necessary to secure the effective coordination of these different types of banking institutions in the Federal Reserve System.

Appreciating fully that the strength of the Federal Reserve System is to be gauged by the quality of its members, rather than by their number, the Federal Reserve Board is prepared to use all the broad discretionary powers vested in itby the Federal Reserve Act to bring about this coordination. The Board has sought, in the regulations governing the admission of State banks and trust companies hereto appended, first, to establish only such reasonable standards of admission as will be generally recognized as necessary to protect the Federal Reserve System against the admission of banks which would be a source of weakness rather than of strength, and, second, to prescribe only such regulations governing their conduct as will insure a reasonable conformity to fundamental principles deemed essential to the success of the new banking system.

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Membership in the Federal Reserve System carries with it privileges and guaranties of great value, not only to the banks themselves, but to their customers as well. It may be confidently expected, provided the standard for admission be kept sufficiently high, that with the further development of the system and the fuller appreciation by the public of its meaning and value, membership in the system will come to be regarded as a test of banking solidity, and that the access afforded by membership, to the facilities and resources of the system, will add to the prestige of even the strongest institutions; so that in time the public in differentiating the banking institutions of the country will, instead of drawing the distinction as in the past between "National banks" and "State banks", rather make the distinction between the banks which belong to the Federal Reserve System and the banks which do not, and ultimately recognize but two classes of banks: "MEMBER BANKS" and "NON-MEMBER BANKS".

The Board realizes, however, that membership in the system also carries with it of necessity obligations and responsibilities as well as privileges and safeguards. The National banks are now, and perhaps will be always, the mainstay of the system: their membership is compulsory, the law having left them no option as to whether they would or would not avail themselves of membership. The main responsibility of the system is theirs and they are therefore fairly entitled to expect that membership of non-national banks shall bring into the system only such institutions as can give substantial promise of being able to share the responsibilities as well as the privileges pertaining to membership.

The Reserve Act, in Section 9, imposes certain fundamental conditions governing the membership of State banks in the Federal Reserve System, and prescribes that banks not organized under Federal law must comply with the

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capital and reserve requirements applying to National banks, and must conform to the provisions of law imposed upon National banks respecting the limitation of liability which may be incurred by any person, firm or corporation to such banks, and of transactions permitted with its directors, the prohibition against purchases of or loans upon stocks of such banks, and the withdrawal or impairment of capital, the payment of unearned dividends, and to such rules as the Federal Reserve Board may prescribe.

With respect to loans on real estate or mortgages, the Board is not disposed to assume as a matter of principle, either the authority or the duty to impose restrictions of a character calculated to embarass State banks in applying for membership, or to impair their usefulness in a field which has been well developed. It has endeavored in the regulations merely to provide a reasonable limitation, so that loans or investments of this character shall not be so excessive in amount as to endanger the liquid condition of a bank.

Within the limits thus described, it will be the policy of the Board to determine the eligibility of State banks for membership in the Federal Reserve System by means of examination. Since admission to the system will be looked upon as an evidence of the bank's strength, examinations for admission must disclose clearly the condition of an applying bank and the character of its management. These examinations must, therefore, be thorough and effective, and be under the direction of the Federal Reserve Board, but the Board will endeavor to avoid any unnecessary additional expense to the banks by dispensing with separate and independent examinations so far as possible and by adopting a method of joint or supplementary examination in conjunction with State banking authorities. The Board plans to draw freely upon the examiners and auditors in the employ of the respective Reserve Banks and to use their services for the purpose of thus supplementing examinations conducted by the banking departments of the several states. It is hoped,

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therefore, that in passing upon applications for membership, the Board and the several Federal Reserve Banks will have the cooperation of State banking authorities, so that every qualified applying bank may be admitted to membership, and all not qualified be excluded.

Membership of State banking institutions in the Federal Reserve System being optional, the Board appreciates that those charged with the management of these institutions might not feel authorized to enter a system which by regulation might restrict the scope of their operations unless a definite assurance were given them of their right to terminate their membership if at any time they should feel it to their advantage to do so. The Board does not apprehend any such development; indeed, it expects that as the system develops membership therein will carry with it guaranties of safety and security which will be of inestimable value. At the same time it recognizes the responsibilities of those entrusted with the management of the State institutions and has, therefore, in the appended regulation, clearly defined the conditions upon which any State institution may withdraw from membership. The Board has taken legal advice from competent sources and has received ample assurances as to its legal powers in this matter. At the same time, the Board has taken the precaution of fixing the aggregate amount that may be withdrawn within any one year so as to fully protect the system in this respect.

Governor.

Secretary

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Tentative Regulation No.____
Series of 1915.

1882 280

F E D E R A L R E S E R V E B O A R D

Washington

STATE BANKS AND TRUST COMPANIES AS MEMBERS OF THE FEDERAL RESERVE SYSTEM.

Statutory Requirements.

The Federal Reserve Act provides:

Section 9. Any bank incorporated by special law of any State, or organized under the general laws of any State or of the United States, may make application to the reserve bank organization committee, pending organization, and thereafter to the Federal Reserve Board for the right to subscribe to the stock of the Federal reserve bank organized or to be organized within the Federal reserve district where the applicant is located. The organization committee or the Federal Reserve Board, under such rules and regulations as it may prescribe, subject to the provisions of this section, may permit the applying bank to become a stockholder in the Federal reserve bank of the district in which the applying bank is located. Whenever the organization committee or the Federal Reserve Board shall permit the applying bank to become a stockholder in the Federal reserve bank of the district, stock shall be issued and paid for under the rules and regulations in this Act provided for national banks which become stockholders in Federal Reserve banks.

The organization committee or the Federal Reserve Board shall establish by-laws for the general government of its conduct in acting upon applications made by the State banks and banking associations and trust companies for stock ownership in Federal reserve banks. Such by-laws shall require applying banks not organized under Federal law to comply with the reserve and capital requirements and to submit to the examination and regulations prescribed by the organization committee or by the Federal Reserve Board.

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

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Any bank becoming a member of a Federal reserve bank under the provisions of this section, shall, in addition to the regulations and restrictions hereinbefore provided, be required to conform to the provisions of law imposed on the national banks respecting the limitation of liability which may be incurred by any person, firm or corporation to such banks, the prohibition against making purchase of or loans on stock of such banks, and the withdrawal or impairment of capital, or the payment of unearned dividends, and to such rules and regulations as the Federal Reserve Board may, in pursuance thereof, prescribe.

Such banks, and the officers, agents, and employees thereof, shall also be subject to the provisions of and to the penalties prescribed by sections fifty-one hundred and ninety-eight, fifty-two hundred, fifty-two hundred and one, and fifty-two hundred and eight, and fifty-two hundred and nine of the Revised Statutes. The member banks shall also be required to make reports of the conditions and of the payments of dividends to the Comptroller, as provided in sections fifty-two hundred and eleven and fifty-two hundred and twelve of the Revised Statutes, and shall be subject to the penalties prescribed by section fifty-two hundred and thirteen for the failure to make such report.

If at any time it shall appear to the Federal Reserve Board that a member bank has failed to comply with the provisions of this section or the regulations of the Federal Reserve Board, it shall be within the power of the said board, after hearing, to require such bank to surrender its stock in the Federal reserve bank; upon such surrender the Federal reserve bank shall pay the cash-paid subscriptions to the said stock with interest at the rate of one-half of one per centum per month, computed from the last dividend, if earned, not to exceed the book value thereof, less any liability to said Federal reserve bank, except the subscription liability not previously called, which shall be canceled, and said Federal reserve bank shall, upon notice from the Federal Re-

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serve Board, be required to suspend said bank from further privileges of membership, and shall within thirty days of such notice cancel and retire its stock and payment therefor in the manner herein provided. The Federal Reserve Board may restore membership upon due proof of compliance with the conditions imposed by this section.

Section 19. If a state bank or trust company is required by the law of its State to keep its reserves either in its own vaults or with another State bank or trust company, such reserve deposits so kept in such State bank or trust company shall be construed, within the meaning of this section, as if they were reserve deposits in a national bank in a reserve or central reserve city for a period of three years after the Secretary of the Treasury shall have officially announced the establishment of a Federal reserve bank in the district in which such State bank or trust company is situate. Except as thus provided, no member bank shall keep on deposit with any non-member bank a sum in excess of ten per centum of its own paid-up capital and surplus. No member bank shall act as the medium or agent of a non-member bank in applying for or receiving discounts from a Federal reserve bank under the provisions of this Act except by permission of the Federal Reserve Board.

Section 21. The Comptroller of the Currency, with the approval of the Secretary of the Treasury, shall appoint examiners who shall examine every member bank at least twice in each calendar year and oftener if considered necessary:

PROVIDED, however, That the Federal Reserve Board may authorize examination by the State authorities to be accepted in the case of State banks and trust companies and may at any time direct the holding of a special examination of State Banks or trust companies that are stockholders in any Federal reserve bank.

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BANKS ELIGIBLE TO MEMBERSHIP

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

(1) It must have been incorporated under a special or general law of the State in which it is located or of the United States (District of Columbia).

(2) It must have an unimpaired capital stock as follows:

In cities or towns of less than 3000 inhabitants, $25,000;

In cities or towns of more than 3,000 but less than 6000 inhabitants, $50,000;

In cities of more than 50,000 inhabitants $200,000.

(3) They must agree to comply specifically with the requirements of the provisions of Sections 9, 19, and 21 of the Federal Reserve Act.

APPLICATIONS FOR MEMBERSHIP

Every State bank or Trust company which shall desire to become a member of the Federal reserve system, shall make

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application on Form____to the Federal Reserve Agent of its district for an amount of capital stock in the Federal Reserve Bank of such district equal to six per centum of the unimpaired capital stock and surplus of such State bank or trust company. Such application shall state that it is made in accordance with a vote of its board of directors, and shall be accompanied by a statement of the conditions of the applying bank certified by an examiner to be approved or designated by the Federal Reserve Board.

Upon receiving the aforesaid application and statement from any State bank or trust company within its district, the Federal Reserve Agent shall submit the same to the counsel of such Federal Reserve Bank, who shall certify that in his opinion membership in the Federal reserve system is not in contravention of the laws of the State or District in which the said bank or trust company shall be located. The application and certificate of counsel shall thereupon be submitted to a committee of not less than three members of the Board of Directors of the Federal Reserve Bank. The said committee shall examine the application and if it shall find that the applying bank has complied with the provisions of this regulation, and is in compliance with the State law, it shall

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transmit the same to the Federal Reserve Board with its recommendations.

APPROVAL OF APPLICATION.

In passing upon applications of State banks and Trust companies for membership in the Federal reserve system, the following considerations will be taken into account.

(1) Whether the assets of the applying bank or trust company are of such a nature as to entitle it to be considered a commercial banking institution in a liquid condition.

(2) Whether the charter provisions and the nature of the powers exercised by the said bank or trust company are or are not consistent with the proper conduct of the business of commercial banking.

(3) Whether or not the statutes of the State or District in which the applying bank or trust company is located, do or do not contain provisions likely to interfere with the proper regulation and supervision of member banks.

Whenever in the judgment of the Federal Reserve Board an applying bank or trust company fully complies with the requirements thus indicated, the said Board will issue

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a certificate of approval of the application, and thereupon the applying bank shall subscribe and pay in its capital stock to the Federal reserve bank of the district in accordance with the corditions provided for member banks.

POWERS AND RESTRICTIONS.

Every State bank or Trust company which shall be admitted to membership in the Federal reserve system, shall conform to the following requirements:

(1) It shall observe all those requirements of the law to which State banks and Trust companies which have become member banks are subject.

(2) It shall conform to at least as high a standard of commercial banking as controlled it at the time of its admission to the system; with such improvements and changes in its banking practice as may have been specifically required of it by the Federal Reserve Board as a condition of the admission.

(3) It shall not engage in loans on real estate or mortgages of a character or to an extent which will impair its liquid condition, and it shall carry in its investments liquid loans eligible for rediscount with the Federal reserve bank to an amount not less than its paid in capital and surplus.

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(4) If in any case such an applying institution has loans secured by its own stocks or loans to one person, firm or corporation aggregating more than 10% of its capital and surplus, it shall adjust such loans to conform with the requirements of the National Bank Act, the same to be done within a reasonable time to be determined by the Federal Reserve Board.

Except as herein specifically provided, every State bank or trust company becoming a member of the Federal Reserve system, shall continue to retain its full rights as a State bank and shall be entitled to exercise all functions permitted by its charter.

Any State Bank or Trust Company which is a member, shall have the right of withdrawal and may withdraw by giving ninety days' written notice of its intention so to do, to the Federal Reserve Bank of the District in which said Bank or Trust Company is located. At the expiration of said ninety days, such member shall surrender all of its holdings of capital stock and it shall be released from its stock subscriptions not previously called. Such shares shall be canceled and the member shall receive therefor a sum equal to its cash paid subscriptions on the shares

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surrendered, and one-half of one per centum a month from the period of the last dividend, not to exceed book value thereof, less any liability of such member to the Federal Reserve Bank; said payments to be made twenty-five per centum (25%) on the expiration of the ninety days' written notice aforesaid, twenty-five per centum (25%) in ninety days, twenty-five per centum (25%) in one hundred eighty days, and twenty-five per centum (25%) in two hundred seventy days after the said first payment; provided, however, that the said Federal Reserve Bank may have the right and option to make the entire payment at any time after the surrender of such stock, provided further, that no Federal Reserve Bank shall be required, in dealing with the voluntary withdrawal of State banks and trust companies, to cancel any stock offered for the purpose of effecting a voluntary withdrawal if such Federal Reserve Bank has previously canceled within the same year ten per centum of its capital stock under the provisions of this regulation. Applications for the voluntary withdrawal shall be dealt with consecutively in the order as they shall be filed. In the case of such voluntary withdrawal of a member bank, the reserve balance kept by it under the provisions of law with its Federal Reserve Bank shall be transferred to the said liquidation account and shall be

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paid off in the same proportions and at the same dates as the repayments of balances due on liquidation account with respect to capital stock.

EXAMINATIONS.

In the matter of examinations of State banks, the Federal Reserve Board expects to cooperate with State authorities in making their examinations and avoid, if possible, duplication of this work. It is proposed to accept the examinations made by States wherever these are found to be thorough and complete and of the same standard as the National bank examination, or else to appoint a representative of the Board or of the Reserve Bank of the District to act with the State examination staff, and in that way enable the Board to accept with confidence the report of the State examiners.

FUTURE REGULATIONS.

The Federal Reserve Board reserves the right to make such amendments and adopt and publish, from time to time, such further regulations as it may deem necessary.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

5/6/15.

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see 192(a) following 290

NATIONAL BANKS ACTING AS

EXECUTOR, TRUSTEE, REGISTRAR, ETC.

Regulation H - Subdivision 5 - Examinations.

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

2 - Regulations provide - that

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

b - The funds, securities and investments in each trust, shall be separate and distinct from the general funds.
1 - Apart and distinct one from another.
2 - Ledgers and books with trust department records shall be entirely separate and apart from the other books and records of the Bank -

Trustee - Personal Trusts

National Banks must account for
a - All securities received
b - Funds received, invested and distributed
c - Income received and distributed.

It may be necessary to examine the trust deed to ascertain the powers of National Banks in making distribution of investment funds.

Investment of Trust Funds

a - May be provided for in the trust instrument itself
b - State law may specify the securities in which trust funds should be invested.
c - The trust instrument may leave the investment of funds to the judgment of the trustee.
d - All securities purchased by the trustee should be listed by the examiner and comments made as to the character of the investments which are purchased. It would be well in this connection to have a com-

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mittee of directors designated to act as a committee on trust funds. All trust funds should be kept invested in order to net a reasonable return.

All securities, mortgages and real estate owned by or purchased for trust estates should be held or registered in the name of the National bank as trustee or executor or guardian as the case may be in order that the securities may not be be confused with those owned by the institution itself.

Records -

Securities held for each Trust should be kept in separate envelopes. Records should be kept in a Personal Trust book of all funds and securities received at the time each trust is undertaken, and all subsequent transactions should be listed in detail. The record should also give a short digest of the powers granted by the Trust in order that ready reference may be made.

Executor or Administrator -

Detailed record should be kept of securities and funds received, of deposit of funds, investments made, whether under authority of law or by direction of the Court. The examination of records should be similar to that of personal trusts.

Escrows -

Securities held under escrow agreements should be checked and accounted for.

Corporation Accounts - Trustee of Bond Issue - Registrar of Bond Issue -

Often the same institution acts as trustee and registrar or transfer agent of a bond issue. The institution should have in its possession the original mortgage or trust indenture, and care should be taken to see that it has been duly admitted to record in the proper court.

Records should show what properties the trust deeds cover, and whether a mortgage is an open or closed one. If a collateral trust mortgage, the underlying trust securities should be accounted for. The trust deed should be examined to see if the bank is acting within its powers.

Sinking Fund Provision -

Securities held for sinking funds should be checked and accounted for. In case of a discrepancy a statement should be sent to the corporation for comparison. The examiner should insist upon proper records being kept in order to facilitate the examination.

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Registrar of Stock Issues -

It will be necessary for the examiner to see -

1 - That proper records are kept of all stock registered by the bank
2 - That proper care is exercised in the issue of new stock
3 - That no new stock is registered unless the old cancelled stock certificates are exhibited to the Registrar.

Securities held for Safe Keeping -

Millions of dollars of securities are held by National Banks for account of and subject to instructions of customers. These securities should be checked in the same manner as personal trusts.

a - Bank records should show the securities the bank is holding and for which account -

These accounts should be carefully checked and verified at least once each year.

Examination of a Trust Department of a National Bank -

The examination of a Trust Department is generally similar to that of a regular bank examination. The safes containing the securities should be sealed - Cash and all other accounts should be verified. Securities held for personal trusts, estates, under escrow agreement or for safe keeping, should be counted and compared with records - Minutes of meeting of Trust Investment Committee or of the Board of Directors with respect to the investment of Trust Funds should be read -

In examination of Corporate Bond issues - all bonds received, delivered and cancelled should be accounted for - Underlying securities and collateral should be counted and compared with records -

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Suggestion for Form -

BALANCE SHEET

Assets -

Investments - Personal Trusts

Cash on hand

Cash on deposit - own bank

Cash on deposit - other institutions

Other assets

Total _____

SINKING FUND

Investments :

Cash for account :

Total _____

Liabilities -

Trust Estates :

Principal Accounts

Income Accounts

Advance to Trusts

Other Liabilities

Total _____

Sinking Fund

Total _____

Sworn Statement of Condition -

On this _____ day of _____ 191 , personally appeared _____ Trust Officer of the _____ National Bank of _____ and made oath, that, to the best of his knowledge and belief, the foregoing statement includes every asset and liability of the trust department of said bank, and is true and correct in all respects.

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Suggestions for Forms Separate Form

BALANCE SHEET - (More complete form)

Resources:

Investments, U. S. Bonds

Municipal and State Bonds

Railroad Bonds

Miscellaneous Securities

Real Estate Owned

Real Estate 1st. Mortgages

Loans - Collateral

Unsecured

Cash on hand

Cash on deposit with Bank

" " " " other institutions

Sinking Fund Investments

Other Assets

Total_____

Liabilities

Trust Accounts

Principal Account

Income Account

Sinking Fund

Other liabilities Total_____

(More detailed statement)

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Schedule -

INVESTMENTS PERSONAL TRUSTS

Descriptions of Security

Rate

Par Value

Book Value

Real Estate - If subject to prior lien - State amount -

Note - If investments are unusual ascertain from trust agreement what classes of investment it authorizes.

TRUST DEPARTMENT

Personal Trusts

I. What officers have been designated by the Board of Directors to act as trust officers?

II. What officers and employees having access to vaults or safes where trust securities are kept?

III. Has the Board of Directors appointed a committee on investment of Trust Funds?

Names of members.

IV. Are all new investments and investment changes reported to and approved by the Board of Directors?

V. What is the general character of the investment made?

VI. Are securities checked from time to time?

Schedule -

PERSONAL TRUSTS

Number of Trust

Name

Principal

Investments

Cash

Income

Remarks

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Schedule -

CORPORATE TRUSTS

Description Bond

Rate

Maturity

Bonds - certified

Uncertified

Cancelled

Total received from issuing corporations

Collateral Security if any

TRUST DEPARTMENT

Corporate Trusts, Etc.

1. Were corporate trust indentures approved by Counsel for bank, before acceptance?

2; Were all bonds, stocks and underlying securities counted and compared with records?

Registrar of Stock Issues.

1. Are proper records kept of all stock registered by the bank?

2. Is proper care exercised in the issue of new stock?

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192 a.

MEMORANDUM FOR DR. WILLIS

Referring to the attached memorandum I beg to hand you herewith an outline of the points which it would be well to have considered in the examination of trust departments of national banks, and also suggestions as to the forms to be used.

The Banking Department of the State of New York in its examination of trust departments uses no special forms. At the conclusion of the examination which is a thorough one, examiner reports simply that the "trust department has been examined and the securities on hand have been found to agree with the records", and he attaches thereto a memorandum of criticisms and suggestions.

On the other hand the State of Massachusetts audits trust departments and use a very complete set of forms. A set of these forms is on file in the Division of Audit and Examination and will be available at any time.

Respectfully,

J. A. BRODERICK

Dated, March 11, 1915.

Approved by

FEDERAL RESERVE BOARD

March 29, 1915.

3/31/15.

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CONFIDENTIAL April 5, 1915. 195.

Circular No. ___
Series 1915.

F E D E R A L R E S E R V E B O A R D.

Permission granted under Section 11, Sub-Section K, of the Federal Reserve Act for National Banks to act as trustee, executor, administrator, and registrar of stocks and bonds.

.....

To Federal Reserve Agents:

In order that the powers of national and State banks and trust companies as members of the Federal Reserve System may be equalized as far as possible, the Board desires to grant to national banks applying therefor, when not in contravention of State or local laws, permission to act as trustee, executor, administrator, and registrar of stocks and bonds. In acting on applications, however, for such permits, it is necessary that the Board should take into consideration,

First: Whether or not the exercise of these powers, or any of these powers, will be in contravention of State or local law.

Second: Whether the applying bank is in proper condition and is equipped to handle this class of business, and whether a permit will, under the circumstances, prove of benefit to such bank.

In order to pass upon the question of whether or not action under the permit will contravene state or local laws, the Board has requested Counsel for the various Federal reserve banks to analyze the laws of the States in the several districts and file his opinion with the Board. In view of the lack of uniformity in the laws of the several States it is difficult, if not impossible, to prescribe any fixed rules by which this question may be determined. Inasmuch as National banks are incorporated under Federal law, the statutes of the various States necessarily have a very limited application, but in this instance Congress has expressly provided that State laws shall not be contravened, just as it did in the case of usury laws of the several States.

There are probably no States whose statutes in terms prohibit National banks from exercising these powers, and few which expressly authorize their exercise. The question under consideration, therefore, cannot be determined by ascertaining merely whether a State law specifically prohibits or specifically authorizes National banks to act as provided by Section 11 (k). Nor is it within the province of the Federal Reserve Board to pass upon the constitutionality of this section. In general, the Board will grant permits in accordance with this section where the exercise of the powers granted does not contravene the general policy of the State laws as indicated

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by the statutes dealing with banking institutions and other corporations, and will refuse permits in those cases where such exercise would be clearly in contravention of the general policy of such State laws.

In determining the second question, that is - whether or not in a given case the granting of the permit will prove to the best interest of the applying bank, the Board must necessarily take into consideration the particular circumstances in each instance. Banks having small capital and surplus should, therefore, be requested to indicate the nature and extent of the business it contemplates undertaking. Its equipment and the efficiency of its organization must of necessity be taken into consideration in determining the general character of the estates to be administered.

While the Board does not desire to promulgate at this time any fixed rules as to the proportion that the capital and surplus of the applying bank should bear to the size of the estates to be handled, it is at once manifest that small institutions should not undertake to administer estates which will require a larger and more efficient trust department than such banks will be justified in establishing. Before making any recommendation, therefore, to the Federal Reserve Board that application should be approved or disapproved, Federal Reserve Banks should give consideration to the circumstances, as indicated above.

It is the desire of the Board to cooperate with the member banks through the Federal Reserve Banks in a gradual and conservative development of this class of business. To this end, applications received by the Federal Reserve Bank should be handled in the following manner :

First : They should be submitted to Counsel for the Federal Reserve Bank, who will certify thereon whether or not, in his opinion, there is reasonable ground for believing that the exercise of the powers applied for will not be in contravention of the laws of the State in which the applying bank is located. The application should then be referred to the Board of Directors of the Federal Reserve Bank.

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Second: The Board of Directors, after due consideration, should forward the application to the Federal Reserve Board with its recommendation. If, for any reason, the directors are of the opinion that the permission applied for should not be granted, the application should be accompanied by its reasons in writing.

Third: The Federal Reserve Board, under the terms of the Act, can authorize national banks to exercise only those powers which are not in contravention of State or local laws, and if, after a permit is granted, the right to act under it should be questioned by the State authorities, member banks should promptly notify the Federal reserve bank and the Federal Reserve Board, so that arrangements may be made for an adjustment or for a proper adjudication by a court of competent jurisdiction.

Circular letter of March 4, 1915 is superseded by this circular.

4/5/15

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We take many things for granted and consider them axiomatic without stopping to consider why. That easy money rates create expansion and that expansion ultimately brings about a reaction accompanied by high money rates, is a doctrine in point. What, however, is the theory underlying this process?

If a country bank has a capital of $20,000 and invests $80,000 of its resources at 5%, it earns $4,000 gross. (Though this equals 20% gross and appears a large return, it may not be excessive if we consider that from this $4,000 there must be paid salaries, rent, etc.). If credit is worth only 2%, this bank will have to invest $200,000 at 2% in order to earn $4,000; and those who cannot put out a larger volume of loans will take chances in making poorer investments, from which liberal returns can always be obtained. In other words, the lower the rate, the stronger the temptation to the banks to act without due caution. The greater the desire of the bank to put out its money, the easier it will be for the borrower to secure over-generous credit facilities, which in turn will lead him to expansion. He may thus be induced to put borrowed money into plant and machinery or into large supplies of goods. When general apprehension

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of over expansion is awakened, or when some additional seasonal or extraordinary demands occur - often demands directly caused by the artificially increased activity - all simultaneously realize that the limit of credit expansion has been reached. A dearth of credit, accompanied by violent contraction and extreme interest rates are the consequences then sure to follow.

It should be the duty of all banks to recognize this sequence of conditions and to govern their conduct accordingly. The large and conservative banks, on which the brunt of the burden falls in case of a general collapse, are fully aware of the danger and try to remain conservative. Nevertheless, in the long run, the spirit of selfishness and competition makes itself felt, and the old adage that "John Bull can stand anything, but he cannot stand 2%" holds good in every country. Against this dangerous tendency to expansion the strongest element of protection is found, when wisely managed, in the large central note-issuing banks. They fulfil their duty of preventing over-expansion by working in time for harder money rates. Either by refusing to do new business they gradually liquidate their holdings of paper or they sell Treasury bills or other securities, accumulating cash against them, or, as is frequently done by the Bank of England, they even borrow in the open market.

Have we in the United States at present conditions that are pregnant with the dangers following great ease of money? With hundreds of millions suddenly released and a future

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highly uncertain, I believe there can be no doubt as to what the conclusions of the Board will be on this point. In order to gain a clear basis for future discussions concerning the policy to be adopted and the best ways and means of carrying it into effect, it is however important that a definite understanding be reached.

Some members of the Board still urge a policy of lower rates; others feel that while it was incumbent on the Board to aid in making money easier, when conditions prevailed such as were originally met, it is now a clear duty not to aggravate the existing plethora of money, but rather to ward off the evil effects certain to follow an over-abundance of credit.

It is my suggestion that a vote be taken on this question and a clear-cut policy agreed upon. Unless this be done, it is impossible to adopt the measures which must be taken from time to time without engaging in endless and fruitless discussions. There must be an understanding on theory and policy before we can pass upon the means of attaining the aims agreed upon.

If, as I suppose to be the case, a majority of the Board does not wish to increase the ease of money at this time, then we must accept these further conclusions :

First : When normal rates fail to bring business to the Federal Reserve Banks we must not try by underbidding to force

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our funds into the investments sought by the commercial banks. As it has been tried to show above, we should otherwise take the responsibility of forcing upon them a policy of either underbidding us or of going into fields of greater hazard. Into these we should be the last to drive them.

Are we then to sit still and not earn our expenses and dividends? What, in that case, would the people say? What will they say if, ultimately, by being short-sighted now, we ourselves should bring about a stringency - the very condition which we are justly expected to guard against? Would it not be better to have the people better informed of our duties and policies? It will not take long to gain the sympathy of those who are most interested in our earnings, the member banks. As a matter of fact, presidents of banks, large and small, north and south, have informed us that they would not be the least disappointed to have the Federal Reserve banks fail to earn their dividends under present circumstances, that they would be amply repaid, even if they received no return on their investment at all, if our system provided safety. They have expressed the hope that we should remain cool and conservative and should not permit ambition for earnings and quick results to tempt the Federal Reserve banks from the wise path of conservatism. I must confess to a feeling of humiliation that our members should have found it necessary to express these feelings to me when such admonition should more properly come from the Federal Reserve Board to them.

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We must reach then a conclusion as to the second question, viz., - is the policy of this Board to be framed according to misconceptions and prejudices prevalent among " the people ", or is it the duty of the Board to educate the people to a better understanding of the broad questions touching finance in general and the problems of the Federal Reserve System in particular ? It might be advisable to take a vote also on this question.

Third : While we have seen what investments we must avoid at the present time,we must on the other hand, consider the positive side of the program of what we may and must do. Before doing that,however, we shall have to undertake one more process of elimination.

If we were not confronted with entirely abnormal circumstances caused by the European war, present conditions would lead Federal Reserve Banks to a policy of investing heavily in foreign bills. Foreign exchange rates are remarkably low and would, therefore, favor such a venture. In addition, by investing in foreign bills, we should withdraw our funds from the home market and thereby exercise an influence in the direction of hardening money rates. We should invest our funds temporarily so as to bring some return from foreign countries. As we should buy only short paper,this would place us in a position,at any time when we should again want our funds for use in our own country, to rediscount the foreign paper thus acquired or to collect it as it matures and to sell foreign exchange against these funds as they

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became available at probably profitable prices. We should use foreign countries, therefore, as a means of steadying our own money rates and should keep these foreign countries as reservoirs to be drawn upon at our will.

Unfortunately, there are very serious objections to our going into that field of operation at this time. As long as the war continues, the holding of the paper of foreign countries involves the danger of laying ourselves liable to any measures that may be taken for their own protection by those foreign countries.

It cannot be foreseen whether this protection will take the form of renewed moratoria or of a refusal to ship gold or of increased prices to be paid for gold by the government banks. It is therefore impossible to foretell with any degree of safety whether a purchase of foreign exchange at this time would be likely to lead to a profit or to a loss. Moreover, the Federal Reserve Banks might subject themselves to severe criticism if they found their funds "tied up" in foreign countries when they wanted to withdraw them, or if they should incur losses in foreign countries, such as might result from critical financial conditions likely to prove to be the consequence of the present turmoil.

Confidential enquiries have elicited the general reply that Federal Reserve Banks would be disinclined at this time to go into foreign exchange transactions or to open the foreign accounts which would be necessitated by such transactions.

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It has been suggested that the Federal Reserve Banks do what the Bank of England would be apt to do under present circumstances; that is to say, borrow money. Such a plan might be carried out by an agreement on the part of the Federal Reserve Banks to pay interest - let us say 2% - on balances of member banks kept in excess of the minimum requirements. Mr. Delano has written a very interesting paper elaborating this thought.

Larger balances thus to be gained by the Federal Reserve Banks would no doubt constitute an important element of protection in dealing with the question of check clearings. It would also remove the opposition of a great many country banks which now object to increasing their balances with Federal Reserve Banks without, on the other hand, receiving on these larger balances the interest they now receive from their reserve correspondents. It is clear that in Central Reserve cities and even to a larger extent in Reserve cities, strong objections would be offered against such a plan which, it might be claimed, would tend to bring about within six months what the law advisedly intended to bring about within two and a half years. Moreover, there is a danger that where once the Federal Reserve

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System begins to pay interest on balances, great pressure will be brought so to amend the law as to force the Federal Reserve Banks to continue doing so. As a broad principle it is unsound to pay interest on reserve money. Interest on reserve money is in itself a stimulus to the employment of reserve money. If, on the other hand, it should not be employed, the Federal Reserve Banks would incur a loss which would curtail the income to be received by the Government, and would, therefore, be a constant opportunity for political attack and interference. While such a policy of paying interest on borrowed money could, with entire propriety, be adopted as an extraordinary measure in time of dangerous ease of money (which normally would drive gold from the country, - a question which it would lead us too far to elaborate here), it would be unsound to adopt such a policy permanently. It is, therefore, not believed that the Board would, or that indeed it should, embark upon a policy of paying interest on excess balances, tempting though this proposal may be in some respects.

Fourth: There remains, however, one large and new field of enterprise heretofore unoccupied by American banking; the bank acceptance, an investment in every respect desirable for

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the Federal Reserve Banks. The American bank acceptance, drawn against the importation or exportation of goods, implies, indeed, at present in most cases, competition not with American, but with foreign banks. Heretofore these transactions have been financed by foreign banks and they have received the commissions for accepting, while the discount markets of such foreign countries have carried the acceptances until they matured. In other words, advances against goods in transit from one country to another were carried by foreign countries. In purchasing these acceptances, Federal Reserve Banks are, therefore, not using reserve money to compete with domestic Banks in domestic credits or domestic investments, but, on the contrary, American is loaned to take the place of foreign, money. Moreover, while the rate of these bank acceptances is low, the business man who secures the credit in order to carry his goods, pays a commission to the accepting bank, plus the discount rate at which he sells the acceptance. A rate of ½% to ¼% for three months, is equal to 1% to 2% per annum. Adding to that a discount of from 2½% to 3% brings the rate at which he secures his money up to between 4% to 5%. There is, therefore, no overstimulation so far as the business man is concerned. Moreover, if properly restricted, acceptances should be given only for

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goods actually sold. The acceptance, therefore, in this case is only a helpful instrument in liquidating a close transaction which matures and ends at a definite time. It is consequently free of the criticism that it stimulates business expansion as might the ordinary credit granted for the general purposes of business.

Fifth: If American banks would give their acceptances (as our Counsel advises us they could) to finance shipments from one foreign country to another, the purchase of such acceptances would, under present conditions, be the ideal investment for Federal Reserve Banks. A transaction of that kind may properly be considered a foreign investment free of the risks of foreign exchange operations. Instead of drawing on London, the Argentine shipper would draw on New York against goods which he had shipped to London. When the bill matures, he must remit to the United States, and if he cannot find bills of exchange on New York to cover the transaction, it is his duty to find gold. He is by contract bound to secure such gold just as, in the fall of 1914, American houses were obliged to send gold to cover their maturing obligations in London, independent of whether or not gold payments had been suspended by the American banks.

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Investments in acceptances of this kind would permit the Federal Reserve Banks to secure a return from some part of their idle money without increasing the ease of money here. Such investments would, indeed, be the best reserve investments because if, within the next ninety days, conditions should change here so as to make it desirable to strengthen our own reserves by putting up the bank acceptance rate, we could force the shipper or the importer to cover his indebtedness, meeting the acceptance and using for his new shipments credits in countries which are willing to offer him lower discount rates. If we put out our money in the United States by investing in so-called American commercial paper, our investment is endowed with very much less of the reserve quality because if the money has gone into investments or plants, we can collect our maturing paper only by forcing the commercial banks of the country to take it over from us. We are only shifting the investment from one American pocket into the other, while if at this time we should finance foreign shipments with our bank acceptances, the liquidation of these acceptances would mean that we should be drawing on the surplus of other countries to strengthen our own. It is this feature of the bank acceptance market which cannot be sufficiently

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emphasized. It possesses an element of elasticity both on account of international relations and on account of the fact that these acceptances can be collected without considering the convenience of the acceptor. This renders the acceptance market the most desirable field of investment for all banks. The larger this market grows and the wider the public it reaches, the safer it becomes and the more readily will the ultimate aim be achieved of making the acceptance market take the place of the stock exchange call money market.

The Federal Reserve System will not be a really safe and efficient organization until the acceptance market is thoroughly developed. It can already be seen that, in the acceptance market, the Federal Reserve Banks will be a controlling factor and, when once sufficiently firmly established, their discount rates for bank acceptances will become not only barometers but, through this agency, important governors, of the money market. It must be borne in mind that the safety of note issuing banks lies in their ability actually to collect and actually to influence money rates.

Our rates for commercial paper will naturally have to remain fairly high because these rates must be granted in every district to the smallest country banks in remote corners, where rates are naturally comparatively high. The

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rediscounting of the long maturity commercial paper will, therefore, be largely restricted to the smaller and weaker banks, and will, therefore, have little direct bearing upon the larger banks whose transactions with their Federal Reserve Banks will probably generally be based on short time paper bearing a lower rate. The most effective money rates will, therefore, be the short term rate and the bank acceptance rate, particularly when, as it is hoped will ultimately be the case, the acceptance covers domestic transactions as well.

It is the bank acceptance that will bring about real fluidity of credit and will serve as an equalizer of money rates all over the country; for the acceptance of a good bank in New Orleans will sell substantially at the same discount rate as the acceptance of a bank in New York, no matter whether the local rate for commercial paper in one district be five and in the other four per cent. If country banks, instead of keeping call money loaned on the stock exchange, are to hold bank acceptances as part of their working reserve, the market for bank acceptances must be wide and reliable, and the more it is internationalized, the more the foreign banks begin to buy our acceptances, and the more we accept in foreign trade, the stronger this market will be and the more perfectly will it

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act as a safety valve should we find it necessary to increase our rate. By accepting for foreign countries, we should be creating a gold reserve which can be quickly marshalled so as to enable us to respond to the commercial demands of the country. At the same time, this reserve would act as a buffer in case exchange should turn against us and the danger of gold exports arise.

Sixth: The sentiment has been quite frequently expressed that we commit an injustice by permitting these low rates for bank acceptances when we could not or would not permit the same low rates for commercial paper. The difference between the two kinds of paper has already been pointed out. Furthermore it must be apparent that we could, of course, lower our rates for commercial paper but that we ought not to do so because such action would be unsound and dangerous. Incidentally, it might be well to consider that if we want to keep our machinery going and want Europe to continue to purchase without bringing about a depletion of gold holdings which might render it impossible for those countries to continue to buy of us, we have to a certain extent to provide the means with which Europe can pay.

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Europe will either sell us back our own securities (which evidently she is not very much inclined to do for the present) or we may give Europe short term credit facilities or buy her issues of securities. To invest our money in European long term securities would not be advisable. The time has not yet come when this country can act as the World's banker and as a permanent investor in foreign securities. Moreover, for political reasons, it is not desirable that large public issues be made here for belligerent powers at this time. On the other hand, should we become the temporary banker of Europe, by granting these acceptance facilities,-a banker who at any time on short notice can call back his funds, - that indeed would be the safest and the most useful position for the United States in present circumstances.

Open market transactions in domestic bills of exchange would have exactly the same effect as a lowering of our bank rates for commercial paper. They would in effect result in competition with the commercial banks in the purchase of commercial paper, such an invasion of their legitimate field of operation would force them to counter the stroke by underbidding us, or - as already shown,- drive them into undesirable investments. The Federal reserve Banks, by taking such a step, would invite the most bitter - and well-deserved - criticism.

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While these two classes of open market operations may appear to be very similar, careful examination will show that the open market purchase of domestic "bills of exchange" would, at this time, weaken our general situation, while the purchase of bank acceptances drawn for foreign account to finance importations or exportations, would add an element of strength.

Seventh: There are now excess reserves of $500,000,000. A loan expansion has already taken place in the past few months of about $220,000,000. There is nothing but the sound common sense of the commercial banks that can prevent a further expansion which may reach to an amount of over $1,000,000,000. The inverted pyramid is likely to grow, but the basis on which the entire structure stands, the reserves, has been reduced by the Federal Reserve Act. Every dollar that the Federal Reserve System puts out at this time further weakens these lessened reserves. The entire safety of the expanded situation rests on the Federal Reserve Banks. At a time at which our usual European credit facilities have become unavailable, and when the European investment markets, on which we formerally relied to a certain extent, have beenclosed, the additional elasticity which our new system provides, is the only means of replacing what thus we have lost. It would appear the part of prudence and sound business judgment to husband our resources and not to increase, but

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rather to counteract, the ease of money which again will drive the banks into fixed investments, These always have proved to be their ruin after a time of great plethora. Within the next two years we must withdraw $200,000,000 from the banks and add this amount to our own resources. Until then, it will be advisable not to let the inverted pyramid grow to an extent which will render it extremely difficult to withdraw such funds. Even if European conditions were entirely normal it would be advisable in these first two years of growth to proceed cautiously. With conditions as they are, there cannot in my mind be any doubt as to our policy.

Trade does not follow the flag unless there is something behind the flag to fasten it to. Trade follows finance as often as finance follows trade. Present conditions - deplorable as they are in many respects - offer us a unique opportunity of establishing ourselves as a financial world power. Now is the time when a friend in need is wanted in all parts of the globe; and when valuable relations can be established with foreign countries.

If we miss this opportunity, if we show hesitation and pettiness where boldness and statesmanship are required, if we cannot get beyond the distinctly local point of view, the

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European countries - when peace will be restored - will remain the masters of the situation as in the past. We cannot be a world power if we do not adopt the broad principle that we must be willing not only to take but also to give, just as other nations are willing to give us the advantages of their facilities whenever, and to the extent that, their own conditions permit. A banker who has the reputation of being essentially selfish will never secure a good class of customers. Our new system can rank with the Bank of England, the Reichsbank and the Banque de France, only if it be administered on broad principles of financial statesmanship and not like a country bank which looks only to what it can earn and seeks to serve only the selfish interests of its immediate customers.

P. M. W.

3-30-15.

P.S. From the point of view of a Federal Reserve Board member- disregarding all other considerations which the Government as a whole must weigh - a sale of United States Government bonds or short term notes would just now have a most desirable effect; provided, that the issue were sold to the public and the commercial banks, the proceeds being actually withdrawn and locked up in the Treasury. It must not be forgotten that the net cash lost by the Treasury during the past few months has gone into circulation and into the banks.

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STATEMENT FOR THE PRESS.

April 6, 1915.

It was announced today at the office of the Comptroller of the Currency, and confirmed by the Federal Reserve Board, that recently published statements to the effect that the Board has under consideration a plan for guaranteeing bank deposits, or that it has considered the subject, were without foundation. The question of guaranteeing deposits has never been raised before the Board in any way whatever, and the Board has had no official information to the effect that the matter was under consideration by any officer of the Government. There is no plan, so far as can be learned, for bringing the subject before the Board for consideration. The Board learned today that sometime ago the Attorney General was asked by the Secretary of the Treasury whether a national bank could legally make a contract with a guaranty company, whereby such company would insure the full payment of deposits in such bank. This inquiry was not made at the instance of the Board and there is no reason for expecting any action by the Board as the result of the Attorney General's reply whatever that may be.

The Comptroller of the Currency added that the newspaper story to the effect that he had devised a plan for the guaranteeing of bank deposits is without foundation; that, as is well known, some national banks in certain sections, for several years past, have had their deposits guaranteed by surety companies. Questions having been raised as to the legality of the method now in use, the Comptroller of the Currency presented the matter to the Secretary of the Treasury, with the request that the Attorney General be asked for an opinion, and this opinion of the Attorney General has just been received by the Secretary of the Treasury and in turn delivered to the Comptroller of the Currency, in response to his original request.

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MEMORANDUM OF SUBJECTS TO BE
Submitted to the
ADVISORY COUNCIL.

First:-

Attention is drawn to Circulars 11 and 12 and to Regulations "J" and "K" in respect to Acceptances (12 copies attached). Are there any further suggestions on this subject?

What is the opinion of the Advisory Council as to the policy of allowing the Federal Reserve Banks to buy the acceptances of State banks and private bankers, regardless of the limitations, when National banks are limited by law to one hundred per cent of capital and unimpaired surplus? A ruling, or even a suggestion by the Board that the Federal Reserve Banks should not buy acceptances of banks beyond the limitations fixed for member banks might at this time be taken as an intended "slap" at trust companies and might later be used as an argument against the Board in the future should it ever advocate the removal of this limitation.

What are the views of the Advisory Council on this question?

Second:-

The Federal Reserve Act provides for the discount or purchase of acceptances based upon the importation or exportation of goods. It has been suggested that importation and

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exportation should not and cannot properly be limited to importation and exportation to or from the United States and its dependencies. What is the view of the Advisory Council on this question ?

Third:

The Federal Reserve Board has under consideration the preparation of a circular and regulation on the subject of the purchase in the open market (under Section 14) of bills of exchange, foreign or domestic. Recognizing, however, that it was of great importance to safeguard these provisions in every way, yet if safely possible, to provide for the purchase of bills of exchange (E. G. documentary bills or bills secured by staples) accepted either by merchants or manufacturers in good standing against goods actually purchased by them. What are the views of the Advisory Council on this question and is it desirable for Federal Reserve Banks to go into the foreign exchange business at this time ?

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Fourth:

The subject of the admission of State banks has been before the Board for several months. On the one hand it is argued that State banks should not be permitted to enter unless they submit to all the conditions that are necessary for National banks; that if more favorable terms are granted to State banks, even if allowable by law, it will be taken as an evidence of weakness or will cause National banks to seek State charters. On the other hand, it is argued that if the rules for admission are drastic, only the smaller and weaker State banks will come in; that strong State banks doing a large commercial business will never come in unless liberal concessions are made, most important among them the privilege of withdrawal from the System on suitable notice. In connection with the whole matter it is suggested by some that an effective clearance system, added to the discount privilege, will be a sufficient attraction to bring in the larger State banks without other concessions. What are the views of the Advisory Council on these questions?

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Fifth:-

Section 19, Paragraphs 164 and 165, read as follows:

> "The reserve carried by a member bank with a Federal Reserve Bank may, under the regulations and subject to such penalties as may be prescribed by the Federal Reserve Board, be checked against and withdrawn by such member bank for the purpose of meeting existing liabilities:
> PROVIDED, however, That no bank shall at any time make new loans or shall pay any dividends unless and until the total reserve required by law is fully restored."

The first part of this paragraph has an important bearing on clearances. Thus far, the Federal Reserve Board has issued no regulations in respect to the proviso. What are the views of the Advisory Council on this subject?

Sixth:-

Does the Advisory Council wish to give any views about the rediscount policy to be followed between Federal Reserve Banks?

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Washington, D. C.

April 8, 1915.

Secretary McAdoo today made public an opinion received from the Attorney General relating to the right of National Banks to have their deposits guaranteed by surety companies. The Secretary referred the question to the Attorney General in response to a request by the Comptroller of the Currency in view of certain questions which had arisen as to the interpretation of opinions given on this subject by the Attorney General in 1908 and 1909. The opinion is as follows:

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"DEPARTMENT OF JUSTICE,

Washington

March 31, 1915.

The Secretary of the Treasury.

Sir:

I have the honor to acknowledge the receipt of your letter of February 12, 1915, enclosing letter of the Comptroller of the Currency, opinion of the acting Solicitor of the Treasury and brief filed with the Comptroller on behalf of a guaranty company and certain national banks, in which the question is raised as to whether a national bank may enter into a contract with a guaranty company under which, in consideration of premiums paid by the bank, the company "insures and guarantees each depositor in the bank the full payment of his deposit therein". You ask my opinion upon this question.

In my opinion, it is within the power of a national bank to enter into such a contract.

The law confers upon national banks such incidental powers as are required to meet all legitimate demands of the banking business, and to enable them to conduct their affairs safely and prudently within the scope of their charters. Section 5136 Revised Statutes; First National Bank v. National

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Exchange Bank, 92 U. S. 122, 127. The power to give security for deposits seems to be recognized by section 5153 Revised Statutes as among these incidental powers. The section last mentioned, after providing that all associations created under the Act, shall, when so designated by the Secretary of the Treasury, be depositaries, further provides that "The Secretary of the Treasury shall require the associations thus designated to give satisfactory security, by the deposit of United States bonds and otherwise, for the safe keeping and prompt payment of the public money deposited with them", etc. It is believed that this section is more reasonably construed as a recognition of the existence of the power on the part of national banks to give security for deposits, than as a grant by implication of authority to give security for government deposits alone.

The power of banks to give security for deposits or for payment of their debts, has been frequently recognized. It has been held that the property of a bank may be pledged as security for a debt, (United States v. Robertson (1831), 5 Pet. 641, 650); that a bond with sureties may be given to prevent depositors from withdrawing their accounts, (Wylie v. Commercial & Farmers' Bank (1902), 41 S. E. 504, 509, 63 S. C. 406), and that a national bank may give its bond with sureties to

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secure a deposit of state funds, (State of Nebraska v. First National Bank of Orleans (1898); 88 Fed. 947, 951).

The power to contract for guaranteeing or securing depositors arises from the nature of the relation existing between the banks and their depositors. The relation created between the bank and a depositor by the receipt of deposits is that of debtor and creditor. National Bank v. Millard (1869); 10 Wall. 152, 155; Davis v. Elmira Savings Bank (1896), 161 U. S. 275, 288. The power to receive deposits, expressly granted to every national bank, (Sec. 5136 R. S.), is, of course, indispensable to the conduct of the business of banking; and the extent of its exercise is in a degree the measure of the success of the bank. The ability of a bank to obtain deposits largely depends upon the confidence of depositors, or the belief that their deposits are secure. Loss of such confidence on the part of depositors is usually attended with loss and inconvenience to them, to the bank and to the public. The law accordingly imposes upon the bank an imperative duty not only to repay deposits, but to keep them secure. For the protection of depositors, its revenues and property are pledged, its stockholders are made subject to a double liability,

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and its directors may be held liable for a violation of their duties.

The means by which depositors are to be protected and secured are not expressly limited or restricted by statute. A large discretion is left to the officers and directors. They may use such means for the purpose as are not prohibited by or inconsistent with the provisions of the law, and as they may reasonably find to be suitable and proper and not inconsistent with the prudent conduct of the affairs of the bank within the scope of its charter. "Whatever protects the depositors", it has been said, "protects the bank because it assures confidence in the bank". Noble State Bank v. Haskell (1908) 22 Okla. 48, 89.

A contract of insurance or guaranty, such as described in the question submitted, may afford protection to depositors by securing the performance of an obligation on the part of the bank which otherwise might not be performed. And it is not unreasonable to believe that such a contract, at the same time, may prove valuable to the bank because of the confidence it may assure. No reason is perceived for prohibiting a national bank, in the discretion of its directors, from so securing its depositors, or for denying to the bank such benefits as they believe may accrue in the form of increased confidence result-

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ing from such a contract.

Opinions of former Attorneys General, dated respectively, July 28, 1908, (27 Op. 37) and April 6, 1909, (27 Op. 272), are referred to in the enclosures as having been construed by the Comptroller of the Currency as holding that national banks are without authority to pay, as part of their legitimate expenses, premiums on policies insuring their depositors against loss.

As I view these opinions, the conclusion in neither of them is inconsistent with the conclusion reached herein. The opinion of July 28, 1908, construing the Oklahoma State Banking Act, determined that a national bank could not lawfully participate in the plan contemplated by the Act for the guarantee of deposits, because it involved essentially a guarantee to the depositors of other banks that they should be paid in full - a contract which was deemed beyond the powers of the bank to make. The opinion of April 6, 1909, held that national banks in the State of Kansas could not avail themselves of the bank depositor's guaranty law of that State. The inquiry, upon the answer to which the decision rests, was, whether an acceptance of the provisions of the Kansas law " would so control the conduct of the affairs of national banks as to expressly conflict with the laws of the United States".

As pointed out in the opinion of the Solicitor of the Treasury, the more recent opinion of May 7, 1909, (27 Op. 324)

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in which the form of a policy of insurance guaranteeing the assets of a national bank against loss was approved, provided certain suggested modifications should be made, is more nearly in point on the question now under consideration, and is in harmony with the views herein expressed.

The language employed in the opinions of July 28, 1908, and April 6, 1909, to the effect that national banks are without power to contract for insuring that depositors shall be paid in full, was used in the course of argument merely, applied to a question which it was not necessary to determine, and may be disregarded so far as inconsistent with this opinion.

Respectfully,

(Signed) T. W. Gregory,

Attorney General."

4/8/15

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FEDERAL RESERVE BOARD

Washington

April 26, 1915.

MEMORANDUM.

Any violation of the provisions of Section 22 of the Federal Reserve Act by officers, directors or employees of a member bank, constitutes a crime, punishable by fine or imprisonment. No ruling or interpretation by the Federal Reserve Board would afford any protection to a person subsequently indicted by a Federal grand jury for any such violation, it not being within the province of the Federal Reserve Board to make an official ruling on the provisions of this section. This opinion, is, therefore, not published as a ruling or regulation of the Board.

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FEDERAL RESERVE BOARD

April 9, 1915.

SUBJECT Section 22 of the Federal Reserve Act.

S I R

As requested by the Board, I have carefully examined and considered that part of Section 22 of the Federal Reserve Act which relates to transactions between a member bank and the officers, directors or employees of such bank. The language which has been made the basis of a number of inquiries, and which the Board is asked to interpret, is contained in that paragraph of the Section which reads as follows.-

> " Other than the usual salary or director's fee paid to any officer, director or employee of a member bank and other than a reasonable fee paid by said bank to such officer, director or employee for services rendered to such bank, no officer, director employee or attorney of a member bank shall be a beneficiary of or receive, directly or indirectly, any fee, commission, gift, or other consideration for or in connection with any transaction or business of the bank Any person violating any provision of this Section shall be punished by a fine of not exceeding $5,000 or by imprisonment not exceeding one year, or both "

Under the terms of this provision any transaction engaged in between a member bank and its directors, officers or employees, which is not excluded from its operation, will constitute a crime and no ruling or interpretation of the Federal Reserve Board which it might attempt to apply to any concrete case would afford any protection to a person subse-

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sequently indicted by a Federal grand jury for any violation of the provision in question. For this reason it does not seem advisable to attempt to express any opinion on the various hypothetical and concrete cases presented for consideration. Inasmuch, however, as there appears to be a wide diversity of opinion as to the proper interpretation and significance of this Section, it may be advisable to analyze, for the benefit of those making inquiries, the provision above quoted in order that the elements necessary to constitute a crime, within the meaning of this Section, may be made a little more clear.

The question for determination appears to be, what class and character of transactions did Congress intend to prohibit as between member banks and their officers, directors and employees.

It will be observed that directors, officers and employees are expressly prohibited from receiving any compensation on account of any transaction except (a) the usual salary or director's fee paid to any officer, director or employee of a member bank, and (b) a reasonable fee paid to such officer, director or employee for services rendered to such bank. Under this language it would seem that for serv-

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ices rendered by directors, officers and employees in their respective capacities of directors, officers and employees proper compensation may be paid, and that in addition where services are rendered in some other capacity a resonable fee may in certain cases be paid for such services. It is, therefore necessary to interpret the language 'for services rendered", in order to determine under what circumstances directors, officers or employees may render services in any other than an official capacity and receive compensation therefor without violating the spirit and intent of the Act.

The Standard Dictionary defines "services" as: "Any work done for the benefit of another, the act of helping another or promoting his interest in any way, hence also a benefit conferred, or use and advantage in general". In 35 Cyc., Page 1434, "service" is defined as "an advantage conferred, that which promotes interest or happiness; benefit". Webster's Dictionary, quoted in Dayton v. Ewart, 28 Montana, 157.

In this connection it must be noted that the courts in construing penal statutes generally give the defendant the benefit of the doubt in cases of ambiguity, and in consequence, the language "for services rendered" would probably be

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given a liberal rather than a restricted meaning. The Court, however, would necessarily consider all the circumstances in each case in order to determine whether the transaction involving such services was intended to be prohibited by the terms of the Act. The rule is clearly stated in the case of the United States v Stern, 17 Fed. Rep. 435, where the Court says.

> "It is a fundamental rule in the administration of criminal law that penal statutes are to be construed strictly, and that cases within the like mischief are not to be drawn within a clause imposing a forfeiture or a penalty, unless the words clearly comprehend the case. In construing a statute we ought undoubtedly to look at the public mischiefs which are sought to be suppressed, as well as the obvious object and intent of the legislature in enacting it, and in doubtful cases these have great influence on the judgment in arriving at its meaning."

And again in Bolles v. Outing Company, 175 U. S. 262 where the Court says.

> "The statute, then, being penal, must be construed with such strictness as to carefully safeguard the rights of the defendant and at the same time preserve the obvious intention of the legislature. If the language be plain, it will be construed as it reads, and the words of the statute given their full meaning, if ambiguous, the court will lean more strongly in favor of the defendant than it would if the statute were remedial. In both cases it will endeavor to effect substantial justice."

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See to same effect :

U. S. v. Wiltberger, 5 Wheat. 75;
U. S. v. Morris, 14 Peters 464;
U. S. v. Buchanan, 9 Fed. Rep. 689;
U. S. v. Hartwell, 6 Wall. 385.

Following the rule laid down in these and other cases it is proper to construe liberally that part of the Act which excepts certain transactions from its operation but the true test in each case would seem to be whether or not compensation has been received in a transaction which may be said to come within what the court describes as " the public mischiefs which are sought to be suppressed. "

Giving a liberal interpretation to the language " for services rendered" it would seem that a director of a member bank may receive, in addition to the usual salary or fee for services rendered as a director, reasonable compensation in those transactions where a bona fide consideration moves from such director to the bank, provided, the transaction is one in which it is proper for him to render such services or to furnish such consideration. Congress clearly intended to prohibit the receipt of any compensation, commission or benefit, either from the bank or from a third party, where the director furnishes no consideration

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to the bank.

A consideration of the law prior to the passage of this Act, and of the "public mischiefs sought to be suppressed," clearly indicates, however, that the sufficiency of the consideration is not the only element involved; and that Congress intended to prohibit not only the payment of fees when no consideration is furnished, but also another class of transactions, namely, those in which the director, by reason of his control of the assets, undertakes to use such assets for his own purposes. In such case the director may furnish a consideration; but inasmuch as he occupies at least a quasi-fiduciary relation as custodian of the funds of others, it may be inferred that Congress deemed it against public policy to permit him to use such funds directly or indirectly for his benefit.

It is unquestionably true that in conservatively managed banks transactions engaged in as between the bank and the directors acting as individuals have resulted in great benefit to the bank. A director connected with other successfully managed corporations may very frequently be the agency through which the bank makes profitable investments, and

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directors having large interests in their banks have in many cases materially added to the earnings of such banks through the agency of other firms or corporations in which they were likewise interested. Consequently, transactions between a national bank and its directors were, prior to the passage of this Act, not made criminal by statute, and, as a matter of fact, were not restricted. On the other hand, to incur a criminal penalty it has heretofore been necessary for the transaction to be of such a fraudulent nature as to constitute misapplication of funds or embezzlement. It is true that under the provisions of the National Bank Act, a director may be punished by fine or imprisonment for making a false entry or a false report with intent to deceive the office of the Comptroller or the public, but in such cases the penalty is based not upon the ground that a prohibited transaction has been engaged in but rather upon the ground that the true status of the bank has been concealed by such false entry or false report.

Under the National Bank Act, the only penalties prescribed for the use of funds of the bank by directors where such use does not amount to misapplication or embez-

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element, are of a civil nature. For example, the directors may be held liable, civilly, where excess loans or loans upon real estate are made and loss results thereby, or, for the violation of any of the provisions of the Act, the Comptroller may institute a suit for the forfeiture of the charter of the bank.

While "directors" have been specifically referred to in the foregoing discussion, analagous principles apply with equal force to transactions involving officers or employees.

It may be assumed, therefore, that Congress intended to restrict transactions between member banks and the officers, directors and employees of such banks, since experience has demonstrated the fact that although the bank may be the beneficiary in many or most instances of such unrestricted transactions, this lack of restriction has afforded a wide field for dishonesty and fraud not punishable by statute or under the common law.

To summarize transactions permitted under the views herein expressed, a director, officer, or employee of a member bank may receive compensation from such bank where services are rendered in his official capacity, or where bona fide

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services are rendered, or an adequate consideration is furnished to the bank by such director, officer or employee acting in his individual capacity, provided the transaction engaged in is not one in which the use of his official position could in any way be instrumental in causing the payment of the fee, commission, gift or other consideration received.

In no case should compensation be received by such director, officer or employee from a third party for services rendered in his official capacity when such compensation results from a transaction between such third party and a member bank.

As above suggested, it is not within the province of the Federal Reserve Board to make an official ruling on the subject under consideration, and the foregoing analysis is intended merely as an expression of individual opinion as to what transactions Congress intended to prohibit by that part of Section 22 which is under consideration.

Respectfully,

(Signed) H. C. ELLIOTT,

Counsel.

Hon. F. A. Delano,
Vice Governor, Federal Reserve Board.

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SYSTEM FOR SETTLING BALANCES

BETWEEN THE FEDERAL RESERVE BANKS.

***

1. A gold settlement fund to be established in Washington

2. Each Federal Reserve Bank to carry a deposit of gold or gold certificates in Washington under the custody of the Federal Reserve Board which will act as the settling agent for the Federal reserve banks. The funds thus deposited to count as reserve for each Federal reserve bank and to be kept by the Federal Reserve Board as a fund for the purpose of settling balances between the Federal reserve banks.

3. Each Federal reserve bank shall maintain two accounts with each of the others, one account showing <u>due to</u> each Federal reserve bank - representing items received from each Federal reserve bank; and the other account showing <u>due from</u> each Federal reserve bank, representing items <u>sent to</u> each Federal reserve bank.

4. Each Federal reserve bank shall telegraph the settling agent by night letter, with mail confirmation, once a week on Wednesday night, and if Wednesday or Thursday is a holiday, on Tuesday night, the amount in even thousands <u>due</u> to each of the Federal reserve banks - these balances to be taken from the account <u>due to</u> Federal reserve banks only. When these telegrams are received, the settling agent will make corresponding debit and credit entries to the accounts of all the

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Federal reserve banks on a settling sheet and thus ascertain the net debit or credit balance of each Federal reserve bank. The settling agent will then telegraph each of the Federal reserve banks in even thousands, the amount of the credits to its settlement account, giving the name of each Federal reserve bank from which each of its credits was received, and also its net debit or credit balance in the settlement. These telegrams to and from the settling agent will be confirmed by letters in form to be submitted by Counsel. Each Federal reserve bank will then know the result of its clearings, and will debit the due to Federal reserve banks' accounts and credit the settlement fund and will credit the due from Federal reserve banks' accounts and charge the settlement fund; the difference between the total debits and credits being equal to the net debit or credit to the settlement fund as advised in the telegram received from the settling agent. The settling agent will then debit or credit the fund of each Federal reserve bank, thus making a settlement at once for the clearings of the week's transactions between the Federal reserve banks.

5. Each Federal reserve bank shall pay into the gold settlement fund $1,000,000 and, in addition, an amount equal to its net indebtedness to all Federal reserve banks. This, on the basis of the last statement, would constitute an initial fund

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of approximately $24,000,000. Each Federal reserve bank will engage to keep at all times a balance in this gold settlement fund of no less than $1,000,000. Excess balances may, at the convenience of each Federal reserve bank, remain deposited with the gold settlement fund. These amounts may be paid in at the Treasury or at any sub-treasury in gold or gold certificates or gold order certificates, arrangements having been made with the Treasury at Washington that it will issue gold order certificates payable to the order of the Federal Reserve Board against amounts so deposited with any sub-treasury or the Treasury. These gold order certificates, it is planned, shall be payable only to the Federal Reserve Board or to any Federal reserve bank. They may be presented for payment at the Treasury at Washington or at any sub-treasury. The Treasury and the Federal Reserve Board will closely cooperate in the matter, and, whenever possible, these gold order certificates shall be payable in gold or gold certificates without any additional charge for transportation wherever presented. It is understood, however, that if, after consultation with the Federal Reserve Board, the Treasury finds it necessary to ship from one point to another in order to have the gold or gold certificates available at the sub-treasury where such certificates are to be presented, the Federal Reserve Board will refund any expense for shipping incurred by the Treasury.

It is the expectation of the Federal Reserve Board and

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the Federal Reserve Banks that excess balances will, as a matter of practice, remain deposited with the gold settlement fund and that gold or gold certificates probably will not be withdrawn except when actually required for special reasons.

6. Cost of operation and currency shipments incurred by the Settlement Fund are to be apportioned by a semi-annual accounting among the twelve Federal reserve banks upon a basis to be later determined in accordance with the relative benefit derived by each Federal reserve bank.

7. Checks drawn on Federal reserve banks to be credited on the basis of time taken to reach their destination according to a schedule to be approved by the Federal Reserve Board.

8. For the first six months of operation of the plan, the fixing of charges for telegraphic transfers of funds for member banks will be left in the discretion of the Federal reserve banks. Such charges shall be made upon the basis of approximate cost and may include the equivalent of an interest allowance for the days involved (as per schedule) for the collection of Federal reserve bank checks. At the expiration of the six months' period, a definite schedule of charges for these telegraphic transfers shall be submitted for the approval of, and shall be determined by, the Board.

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AVERAGE TIME TO DESTINATION BETWEEN FEDERAL RESERVE BANKS

	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
Boston		1*	1*	2	2	3	2	2	3	3	4	6
New York	1		1	2	1	2	2	2	2	2	4	6
Philadelphia	1*	1*		1	1	2	2	2	2	2	3	6
Cleveland	2*	2*	1*		2	2	1*	2	2	2	3	5
Richmond	2*	1*	1*	2		2	2	2	2	2	3	6
Atlanta	3*	2*	2*	2	2		2	2	2	2	2	5
Chicago	2*	2*	2*	1	2	2		1*	1	1	2	4
St. Louis	2*	2*	2*	2	2	2	1*		2	1	2	4
Minneapolis	3*	2*	2*	2	2	2	1*	2		2	3	4
Kansas City	3*	2*	2*	2	2	2	1*	1*	2		2	4
Dallas	4*	4*	3*	3	3	2	2*	2*	3	2*		3
San Francisco	6*	6*	6*	5	6	5	4*	4	4	4	3	

(*) Indicates that it is left to discretion of bank to apply less number of days in case it may from time to time find this advisable.

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Washington, D. C., April 16, 1915.

Dear Mr. Clemens:

I have received a letter from Mr. L. C. Irvine suggesting that I give you an outline of a plan for a system of rural credits in Alabama that was discussed at a meeting of the Alabama Land Congress at Mobile, in the fall of 1912.

I wish to say that the subject of rural credits is one that does not properly come within the purview of the Federal Reserve Board, and at the last session of Congress a joint committee was appointed, as you know, to consider the subject and report to Congress at its regular session next winter. What I have to say, therefore, must not be regarded as an expression of the views of the members of the Board, or as having any official significance whatever, as I am writing purely as a citizen of Alabama who feels a deep interest in the development of our State along all legitimate lines.

The events of the past six months have demonstrated in a forcible way the necessity for crop diversification, and have shown the great advantages that would be gained by the division of large plantations into smaller farms actually owned by those cultivating them, thus correcting the evils of absentee landlordism. Our State enjoys great natural advantages as to soil and climate, and should attract thousands of desirable settlers from abroad and from other states. It is important also in order to secure the best results, that farm life be made more attractive. The chief obstacle in the way of the proper development of our rural communities in Alabama has been the lack of money at reasonable rates, and this circumstance has been one of the principal factors in making us so dependent upon a single crop. Our present credit system practically forces the production of cotton to the virtual exclusion of all other money crops, and year after year we have seen a large part of the money which comes into the State for the purchase of cotton go out again to pay for foodstuffs, including both grain and meat. Some headway has been made in recent years in the production of corn, and in a few localities the live stock industry has shown signs of promise. Vast tracts of land, however, are planted in cotton every year or are permitted to lie fallow, that are admirably adapted for cereals, for potatoes, for sheep grazing or for cattle raising. Even in the production of cotton our methods are in most cases crude, and as a rule our farmers are not able to adopt the advanced systems that obtain in other sections of the country, which are less favored by nature.

I am sure that there are many tenants who would be glad of an opportunity to become landlords, and that there are many small landlords who would like to diversify and to adopt more scientific methods of farming, if they could make the necessary financial arrangements; but going into debt is a serious thing, and the idea of a loan of a few hundred or a few thousand dollars for two or three years at a high rate of interest secured by a mortgage upon the farm, which is at the same time a homestead, is not attractive. It would mean in many cases the shifting of

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the loan at maturity, or a foreclosure; but if loans to run 25 or 30 years could be had, repayable in annual installments which would be less than ordinary interest payments under present conditions, the whole aspect of the case would be changed.

The Federal Reserve Act, which has revolutionized the financial system of the country, does not provide, as far as the public is concerned, any new banks of deposit or discount. It merely created a coordinated system of banking, and established for the use and protection of banks already in existence, twelve additional banks.

The interest in rural credits, while widespread, is not as great in some sections as in others, nor is the need for such a system in some of the older and wealthier states, as great as is the case in the south. It seems to me that the question is essentially one for consideration by the states, and that if there were land banks established in several states, that a basis would thus be afforded the National Government for its cooperation.

The legislature of Alabama will convene again in July to consider a plan for the permanent relief of the State treasury as proposed by Governor Henderson, which will, if adopted by the legislature, call for the submission to the people of an amendment to the Constitution. The rural credit plan discussed at the Alabama Land Congress would also require, to become effective, an amendment to the Constitution.

It seems to me, therefore, that the time is opportune for the serious consideration of some adequate plan for the safe and proper development of our farming districts. It is not proposed that the State should engage in the banking business; that experiment was tried 90 years ago and resulted 15 years later in disaster. Nor is it suggested that our laws be changed so as to encourage wild speculation in lands, or to permit the operation of irresponsible or mushroom organizations. The banks of Alabama have done a great deal for the development of the State, and many of them make loans on real estate. These banks all use for this purpose funds on deposit with them on which in most cases interest is paid. Their terms, therefore, are necessarily not as liberal, both as regards the duration of the loan and the rate of interest, as are desirable, and if every farm mortgage loan now carried by Alabama banks should be repaid, there should be no difficulty in employing these funds to good advantage in building up the commercial interests of the State. I hope, therefore, that after the plan proposed is carefully studied, and if it should be found to be sound and practicable, that it will not be opposed by the banking interests of the State. It is thought that its adoption would relieve them of fixed loans, that it would at the same time develop a broader field for desirable temporary loans, and would furthermore tend to increase deposits.

The plan suggested would call for the incorporation and organization of a land mortgage bank to be located in such city as may be determined by the legislature, with a paid in capital of say $500,000, and with an authorized capital of five or six times that sum. As private lenders are exempt from taxation on mortgage loans after the record fee

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of $1.50 per thousand has been paid, it would be necessary in order to secure subscriptions to the capital stock, to exempt shares of stock in the land mortgage bank from taxation. It would be well to have the stock as widely scattered over the State as possible, and, therefore, a tentative allotment should be made to citizens of each county in proportion to its population. Should the citizens of any county fail to subscribe for the full amount allotted them, the balance could be taken by citizens of other counties.

The land mortgage bank should not be permitted to receive deposits of any kind, and its operations should be limited to the investment of its own capital and of the funds secured by a pledge of its mortgage loans. Large profits should not be permitted to be a consideration, all loans should be made at rates of interests as reasonable as possible, and the expenses of administration should be kept down as far as may be consistent with efficiency. It is suggested, therefore, that dividends to stockholders be limited to six per cent per annum, and that the balance of earnings, after carrying a small part to surplus, should be paid over to the State for the school fund, for the construction of good roads, or for such other purposes as may be determined by the legislature.

Great care should be taken in passing upon applications for loans, which should be limited to farms in cultivation upon a basis of not exceeding 50% of actual values, and reference should be had to the books of the county tax assessors in determining these values. So far as possible, applications should bear the approval of two or more stockholders of the land bank residing in the county where the property is located. Competent actuaries should be consulted in order that the annual payments, which should include the interest charge and the amortization payment, may be scientifically correct. It might be well to authorize the tax collectors in the various counties to collect these payments for the land bank at the time the taxes on the property are paid.

When the funds provided by the paid in capital stock shall have been exhausted, the land bank should be authorized to deposit its mortgages with a trustee to secure an issue of collateral trust bonds, the proceeds of which should be used for additional loans. The total issue of collateral trust bonds should not exceed four or five times the actual paid in capital, so that if the land mortgage bank should begin business with a capital paid in of $500,000, its maximum limit of collateral trust bonds would be $2,500,000. After that figure is reached, it would be necessary to increase the capital stock before making additional loans. A proper proportion of these bonds, represented by the amount of amortization payments, should be retired annually. In order to secure the best results, and to enable these collateral trust bonds to have the widest possible market and to command the lowest rate of interest, the State should guarantee payment of principal and interest. This suggestion I know is sure to meet with some opposition. It seems to me, however, that the interests of the State could be thoroughly safeguarded, and that its margin of security would be ample. In the first place, the loans would be well scattered; next, the State would have in its own hands the collection of the interest and amortization installments that would become due each fall; and third, it should have a share in the

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management of the bank by providing that not more than two-thirds of the directors should be chosen by the stockholders, and that at least one-third should be appointed by the Governor to represent the State; or it might be provided that certain State officers, elected by the people, should be ex-officio directors of the land mortgage bank. Furthermore, should the total amount of collateral trust bonds to be issued, be limited to four or five times the paid in capital of the land mortgage bank, the State would always have a margin of at least 20 per cent for its protection, represented by the amount of the paid up capital.

The legislature of the State of South Carolina recently enacted a law providing for a system of state warehouses. Receipts for cotton stored in these state warehouses are supported by the faith and credit of the State, and I am informed, are readily accepted as collateral for loans, both within and without the State, at very low rates of interest. Perhaps it might be well to adopt a similar warehouse system in the State of Alabama, but this reference is made merely to show the effect of a state guaranty. I think there is no doubt that a bond, secured by well selected mortgages, bearing a low rate of interest and guaranteed by the State of Alabama,would be eagerly sought by investors. Probably the bulk of such an issue would be absorbed by local money savers.

I am of the opinion that should a system be worked out along the lines suggested above, that the land mortgage bank could afford to make farm loans, running approximately 25 years, at an annual rate, including the amortization, of not exceeding the straight legal rate of interest in Alabama. An encumbrance of this kind, besides providing means for crop diversification and for the improvement of farms, would really make more saleable the farm so mortgaged. For instance, suppose that a farmer who had carried his loan for five years desired to sell his place,- the purchaser would merely pay him his equity, and assume the remaining 20 annual payments. A system of this kind, properly operated, would greatly increase taxable values throughout the State, and should our legislature look with favor upon this idea, it only would be following in the footsteps of other states that have already contributed both of their resources and of their credit to the up-building of their agricultural communities.

The objection will probably be urged that this would be class legislation, but as a constitutional amendment would be necessary for it to become effective, the system could be adopted only by a majority vote of the people, which would demonstrate that the legislation is after all not for a class, but for the best interests of a majority of the people of Alabama. If not adopted, no harm would be done, as an election would have to be held in any event should the legislature adopt Governor Henderson's views regarding permanent measures for relieving the finances of the State.

I do not wish to be understood that a guarantee by the State of the collateral trust bonds to be issued by the proposed land mortgage bank is absolutely essential for the success of a rural credit system in Alabama. Exemption of the stock of such a bank, however, from all taxation whatever, is, from the reasons already cited, absolutely necessary. It

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may be that State supervision and close cooperation between the State officials and stockholders of the land mortgage bank, and the good quality of the loans in which its capital stock would be invested, would be enough to inspire sufficient confidence in the bank's collateral trust bonds to make them marketable at a fair rate of interest, by no means as low, however, as would be the case if the bonds were supported by the credit of the State. I appreciate moreover, the dangers that would attach to the policy of making the State the guarantor of obligations indefinite as to amount, and am of the opinion that in case it should be decided to submit the ideas above advanced to the legislature, it might be well to limit the total issue of bonds to be guaranteed by the State to a fixed sum, say $2,000,000, which would, on the basis of a paid in capital of $500,000, give the State a margin of 25%. After this amount had been invested in farm mortgages, the system would have then been tested out and understood, and if proved a success, further bond issues could be floated on satisfactory terms without recourse to the credit of the State.

There are doubtless many legal matters which should be considered in this connection, which I as a layman am not qualified to discuss. The object of this letter is to sound the sentiment in Alabama as regards rural credits, and should the idea arouse any interest it might be well to submit the entire question to the consideration of the various commercial bodies in the State, in order that the details may be worked out, that the legal questions may be duly considered, and that a bill may be drawn by competent counsel.

Very truly yours,

W. P. G. Harding.

Mr. W. M. Clemens, Managing Editor,

The Mobile Item,

Mobile, Ala.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

April 19, 1915.

Subject: Legal Reserve - Federal Reserve Banks.

S I R :

In connection with the plan now under consideration under which the Federal Reserve Board contemplates assuming the functions of a clearing house for the several Federal reserve banks, this office has been requested to give an opinion on the following questions:

1. Whether gold kept in a clearing fund under the control of the Federal Reserve Board may be counted by Federal reserve banks depositing such gold as part of their reserve against liabilities other than Federal reserve notes.

2. Whether any part of such clearing fund may be kept by the Federal Reserve Board in the Treasury or one of the Subtreasuries of the United States.

In reference to the first question, Congress has not in terms defined by statute what constitutes reserve against demand liabilities and in order to reach a conclusion as to what may or may not be counted as part of such reserve, it is necessary to review and interpret the principal acts of Congress dealing with this subject.

The Act of June 3, 1864, being Revised Statute, Section 5191, provided in part as follows:

> "Every national banking association in either of the following cities * * * * shall at all times have on hand in lawful money of the United States, an amount equal to at least twenty-five per centum of the aggregate amount of (its notes in circulation and) its deposits; and every other association shall at all times

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have on hand in lawful money of the United States, an amount equal to at least fifteen per centum of the aggregate amount (of its notes in circulation and) of its deposits."

The same Act further provided, (Section 5192) that :

"Three-fifths of the reserve of fifteen per centum required by the preceding section to be kept, may consist of balances due to an association, available for the redemption of its circulating notes, from associations approved by the Comptroller of the Currency * * * * and doing business in the cities of * * * *. Clearing-house certificates, representing specie or lawful money specially deposited for the purpose, of any clearing-house association, shall also be deemed to be lawful money in the possession of any association belonging to such clearing-house, holding and owning such certificate, within the preceding section."

The Act of June 20, 1874, provided as follows :

Section 2: "That section thirty-one of 'the national bank act' be so amended that the several associations therein provided for shall not hereafter be required to keep on hand any amount of money whatever, by reason of the amount of their respective circulations; but the moneys required by said section to be kept at all times on hand shall be determined by the amount of deposits in all respects, as provided for in the said section."

Section 3: "That every association organized, or to be organized, under the provisions of the said act, and of the several acts amendatory thereof, shall at all times keep and have on deposit in the Treasury of the United States, in lawful money of the United States, a sum equal to five per centum of its circulation, to be held and used for the redemption of such circulation; which sum shall be counted as a part of its lawful reserve, as provided in section two of this act."

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It will be observed from the foregoing that prior to the Act of June 20, 1874, no distinction was made between reserve required to be held against circulating notes and that required against deposits and this amendment relates only to the amount, and not to the character of reserve required.

Analyzing the provisions quoted above, it appears that reserve required by law before the passage of the Federal Reserve Act might consist of

(a) Lawful money on hand

(b) Balances due from approved Reserve agents

(c) Clearing House certificates, representing balances due from Clearing House Associations.

(d) Five per cent redemption fund, which consists of lawful money deposited with the Treasurer of the United States for redemption of circulating notes.

In other words, from such analysis, it seems that reserve may reasonably be defined as lawful money on hand or so deposited, in accordance with law, as to be available at all times for the discharge of liabilities against which it is held. For example, lawful money on hand is available to meet demands made at the bank. Balances due from approved Reserve agents are available to meet those liabilities which can be discharged by checks or drafts drawn against such approved Reserve agents, even more satisfactorily than by the actual shipment of lawful money or such balances can be immediately converted into lawful money to meet demands made at the bank.

Clearing House deposits are available to meet demands presented through the Clearing House and the five per cent redemption fund is available to redeem circulating notes presented to the Treasurer of the United States.

The Federal Reserve Act repeals that part of the Act of June 20, 1874, which permits National banks to count the five per cent redemption fund as part of their legal reserve, but does not otherwise amend any provisions of law relating to the character of reserve to be held against deposits. It provides that a gold reserve shall be maintained against liabilities for Federal reserve notes and a reserve of gold or lawful money

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against deposits in Federal reserve banks.

It does not otherwise define in terms legal reserve.

Section 16 of the Act reads in part as follows:

> "Every Federal reserve bank shall maintain reserves in gold or lawful money of not less than thirty-five per centum against its deposits and reserves in gold of not less than forty per centum against its Federal reserve notes in actual circulation," etc.

The Act does not provide, except by implication, where the reserve held against deposits shall be actually carried. The reserve against circulating Federal reserve notes, however, under the terms of the Act, is to be carried partly in the vaults of the bank and partly with the Treasurer of the United States in order that notes presented for redemption to the Treasurer may be redeemed out of the funds furnished by the Federal reserve banks.

Section 16 of the Federal Reserve Act provides in part that :

> "The Federal Reserve Board * * * * may at its discretion exercise the functions of a clearing house for such Federal reserve banks."

One of the principal functions of a Clearing House is to act as a depositary of funds of its members to be held for the discharge of liabilities of such members, which are presented to the Clearing House.

By analogy, therefore, if funds deposited with the treasurer of the United States for the redemption of Federal reserve notes are to be counted as part of the legal reserve of Federal reserve banks, required to be maintained against such notes, it would seem entirely consistent to count funds deposited with the Federal Reserve Board for the discharge of its deposit liabilities as part of the legal reserve required to be held against such deposits.

Such a fund not only meets the general requirements of lawful reserve, as indicated by the Acts referred to, but inasmuch as clearing house certificates

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are specifically authorized by statute to be counted as part of the lawful reserve of National banks and the Board is authorized to act as a clearing house for Federal reserve banks, it would seem that its certificates would come within the spirit of the Act. In other words, while Section 5192 relates to the reserves of National banks, the Federal Reserve Act makes no distinction between the character of reserve of such banks and the character of reserve of Federal reserve banks.

In answer to the second question, while the Act does not in terms provide for deposits by the Federal reserve banks, or by the Federal Reserve Board, with the Treasurer of the United States, the Attorney General has rendered an opinion on the status of the Federal Reserve Board, in which he holds that the Board is an independent establishment and the members are officers of the United States.

As such officers, it is entirely consistent with the established practices of the Government that accounts should be opened with the Treasurer or Assistant Treasurer for the deposit of any funds held by the Federal Reserve Board. In other words, since that fund will be deposited with the Federal Reserve Board and since the Board at this time is without the necessary facilities for keeping such fund, the Treasury of the United States would seem to be the proper place for its deposit.

The bookkeeping incident to handling the clearings, could of course be handled by the Board without reference to the physical location of the funds in question.

I am, therefore, of the opinion that both questions may be answered in the affirmative.

Respectfully,

(Signed) M. C. ELLIOTT,

Counsel.

Honorable F. A. Delano,
Vice Governor, Federal Reserve Board.

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Tentative

Circular No._____
Series of 1915.

FEDERAL RESERVE BOARD

Washington, April 26, 1915.

The Purchase of Bills of Exchange in the Open Market.

As is perhaps generally known, one of the important objects of the Federal Reserve Act was the establishment of a broad "discount market" which would to a large extent supersede the "call money market." In the regulations already promulgated, substantial progress has been made in its establishment by providing for the purchase or rediscount by the Federal Reserve Bank of commercial paper endorsed by the member bank offering it, or the purchase by the Federal Reserve Banks of acceptances growing out of import or export of goods, whether indorsed or not. The object of the present circular is to arrange for a still further enlargement of this business by providing for the discount by member banks of domestic bills of exchange, whether accepted by bankers or by merchants, manufacturers or industrial corporations in good standing, and their rediscount or purchase in the open market by Federal Reserve Banks.

Among the monographs presented by the National Monetary Commission in 1908-09 is one on the Discount System in Europe, in which the following paragraph appears:

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(b) That no bill is "eligible" the proceeds of which have been used or are to be used:

(1) For permanent or fixed investments or any kind, such as lands, buildings, machinery (including therein additions, alterations, or other permanent improvements, except such as are properly to be regarded as costs of operation). It may be considered as sufficient evidence of compliance with this requirement if the maker or drawer shows, by statement or otherwise, that he has a reasonable excess of quick assets over his current liabilities on open accounts, short-term notes, or otherwise;

(2) For investments of a merely speculative character, whether made in goods or otherwise.

III.

Method of certifying eligibility.

Any domestic or foreign bank, firm, corporation or individual, offering a bill for sale to a Federal Reserve Bank shall certify in writing that the bill was issued for one of the purposes mentioned in the above paragraphs and conforms to section 13 of the Federal Reserve Act and to this regulation.

Every such bank, firm, corporation or indicidual shall furnish an original signed statement of the financial condition of the maker or drawer of the bill, or true copies thereof, certified by a notary public, designating where the original statement is on file. Statements should contain all the information essential to a clear and correct knowledge of the maker's or drawer's credit and of his method of borrowing. A schedule specifying certain information, which it is desirable that such statements should include, is hereto appended.

Statements of the maker's or drawer's financial condition may be waived in the following cases:

(1) If the bill bears the acceptance of the purchaser of the goods and presents prima facie evidence that it was issued for goods actually sold, or

(2) If the bill be specifically secured by documents covering readily marketable staples.

In order that bills of exchange eligible for discount under these regulations shall be readily identified, it is very desirable that the Federal Reserve Banks shall adopt a standard form of bill which shall show in a simple and readily recognizable way the "payer", the "payee", the "acceptor", the "indorser" and the invoices covered by the acceptance. Such forms have been submitted to the Federal Reserve Board,

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but in the opinion of the Board it is proper to leave the working out of details of this kind with the Federal Reserve Banks.

CHARLES S. HAMLIN,
Governor.

H. PARKER WILLIS,
Secretary.

APPENDIX

INFORMATION DESIRED OF MAKERS OR DRAWERS.

The credit files of Federal Reserve Banks should include information concerning the following matters:

(a) The nature of the business or occupation of the maker and acceptor of purchased bills;

(b) If an individual, information as to his indebtedness and his financial responsibility;

(c) If a firm or corporation, a balance sheet showing quick assets, slow assets, permanent or fixed assets, current liabilities and accounts, short-term loans, long-term loans, capital and surplus;

(d) All contingent liabilities, such as indorsements, guaranties, etc.;

(e) Particulars respecting any mortgage debt and whether there is any lien on current assets;

(f) Such other information as may be necessary to determine whether the borrower is entitled to credit in the form of short-term loans.

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Federal Reserve Bank of St. Louis

Tentative Regulation_____
Series of 1915.

FEDERAL RESERVE BOARD.

Washington, April 26, 1915.

The Rediscount by Federal Reserve Banks or Purchase of Bills of Exchange in the Open Market.

The word "bill", when used in this regulation, shall be construed to include only bills of exchange, and the word "goods" shall be construed to include goods, wares, merchandise, or staple agricultural products, including live stock.

I.

Statutory Requirements.

The Federal Reserve Act provides that a bill, other than an acceptance, to be eligible for purchase by a Federal Reserve Bank, must comply with the following statutory requirements:

(a) It must have a maturity at the time of discount of not more than 90 days, except as provided by Regulation C, accompanying Circular No. 4, series of 1915, in regard to six months agricultural paper.

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

(c) It must not have been issued for carrying or trading in stocks, bonds or other investment securities except bonds and notes of the Government of the United States; but the pledge of goods as security for a bill is not prohibited.

II.

Character of paper eligible.

The Federal Reserve Board, exercising its statutory right to define the character of a bill eligible for purchase by a Federal Reserve Bank, has determined:

(a) That it must be a bill representing the production or manufacture of certain definite articles or commodities, having a recognized standard of character and readily salable quality; the object being to have the paper represent salable and self liquidating transaction independent of the maker, acceptor or endorser of the note.

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> "There are, then, two primary kinds of bills in use in Europe - the one drawn by the producer, manufacturer, or trader on his respective purchaser and accepted by the latter, and the other, the bill drawn on and accepted by a bank or banker."

In circulars and regulations already promulgated, the purchase or discount of the second form of bill of exchange herein described has been provided for, and it therefore remains for us now to provide for the purchase of the first mentioned form of bill of exchange. This form is generally known to bankers as the "trade acceptance" in contradistinction to the "bankers' acceptance."

Section 13 of the Federal Reserve Act provides in part as follows:

> "Upon the indorsement of any of its member banks, with a waiver of demand, notice and protest by such bank, 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 Federal Reserve Board 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; 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 ninety days: Provided, That notes, drafts, and bills drawn or issued for agri-

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> cultural purposes or based on live stock and having a maturity not exceeding six months may be discounted in an amount to be limited to a percentage of the capital of the Federal reserve bank, to be ascertained and fixed by the Federal Reserve Board.
>
> The aggregate of such notes and bills bearing the signature or indorsement of any one person, company, firm, or corporation, rediscounted for any one bank shall at no time exceed ten per centum of the unimpaired capital and surplus of said bank; but this restriction shall not apply to the discount of bills of exchange drawn in good faith against actually existing values."

Section 14 of the Federal Reserve Act provides in part as follows:

> "Any Federal Reserve Bank may, under rules and regulations prescribed by the Federal Reserve Board, purchase and sell in the open market at home or abroad, either from or to domestic or foreign banks, firms, corporations or indiciduals, cable transfers and bankers' acceptances and bills of exchange of the kinds and maturities by this Act made eligible for rediscount, with or without the endorsement of a member bank."

The rediscount of bills of exchange referred to in the foregoing paragraphs has been provided for in Circular #3 and Regulation "B", series of 1915, which, as already stated, covers the rediscount not only of bills of exchange, but of notes and drafts as well. (i.e. these are all classed as forms of "commercial paper").

The rediscount of "bankers' acceptances" or their purchase in the open market have likewise been provided for in Circular No. 5 accompanied by Regulation "D".

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The purchase of bills of exchange in the open market remains to be provided for. The language of the Act above quoted makes it evident that all bills of exchange which are eligible for rediscount are likewise eligible for purchase by Federal Reserve Banks, subject to regulations of this Board with or without the endorsement of a member bank, whether they are the acceptances of bankers or of merchants or manufacturers in good standing. Regulations which apply to the rediscount of bills of exchange (e.g., commercial paper) should consequently apply to the purchase of bills of exchange, except that the intervention of a member bank as the sole source through which such bills may be presented to a Federal Reserve Bank is eliminated, while the requirement that the indorsement of a member bank be placed upon such bills is likewise eliminated and such portions of the regulations relating to rediscount as grow out of the indorsement requirement may, therefore, be dispensed with. At the same time, it should be borne in mind that a bill of exchange in proper form, bearing the indorsement of a member bank, may be used as collateral for Federal Reserve Notes, while those not so indorsed can not be so used.

The accompanying regulation consequently follows the language of Regulation "B" attached to Circular #3, series of 1915, except in so far as departure is rendered necessary by the considerations set forth above.

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It is not the conception of the Board that the above described bills of exchange or trade acceptances shall supplant or take the place of other approved forms of borrowing. It is most desirable that the manufacturer or producer shall make his own financial arrangements and borrow on the strength of his own credit and the statement which he is able to make, as provided in Circular No. 3, Regulation "B", and the above described bill of exchange simply supplements the former by introducing a form of two-name paper which is much used in Europe and was formerly much used in this country, as an alternative method. It should be safeguarded so as to represent the highest possible grade of domestic paper, supported not only by the good name of the maker of the bill, and the acceptor, (in some cases even by indorsement) but also by the value of readily salable commodities which it should represent.

(Signed) Charles S. Hamlin
Governor.

(Signed) H. Parker Willis
Secretary.

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TREASURY DEPARTMENT

Washington, April, 23, 1915.

Office of
Commissioner of Internal Revenue

M. C. Elliott, Esq.,
Counsel, Federal Reserve Board,
Treasury Department,
Washington, D. C.

S I R :

This office is in receipt of your letter of the 17th instant propounding a number of inquiries concerning the application of the Act of October 22, 1914, to various documents required under the operations of the Federal Reserve Act. Answers follow herewith numbered in accordance with the numbers given by you to the questions contained in your said letter.

(1) While this office understands them to be required by express provision of the Federal Reserve Act, certificates made to the Comptroller of the Currency by Federal Reserve Banks showing increases or decreases in capital stock, appear to fall directly within the exemption contained in the paragraph of T. D. 2087 issued by this office, entitled "Certificates for use of the Government," covering among other documents "Reports made to the Comptroller of the Currency." It is therefore held that no tax stamps are required on these certificates.

(2) Certificates not required by any express provision of law, but merely under the regulations of the

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Federal Reserve Board acting under general authority conferred by law are not subject to tax under the Act here in question. In this connection attention is invited to the first two paragraphs of T. D. 2087, copy of which is enclosed herewith.

(3) It being the understanding of this office that Federal Reserve Banks are held to occupy the status of private rather than public institutions, certificates of stock when issued by them, are held to be subject to tax under paragraph 1 of schedule A of the Act of October 22, 1914, imposing taxation in the amount of five cents per $100 of face value or fraction thereof, upon original issue of certificates of stock by any company, association or corporation. This office holds the face value of such certificates to be the par or nominal value of the stock covered thereby, even though the certificates show upon their face that only part of the full price has been paid therefor.

(4 & 5) This office is aware of no provision of law under which tax could be imposed upon interim receipts given by Federal Reserve Banks for individual assessments on stock subscriptions.

Respectfully,

(Signed) W. H. OSBORN,

Commissioner.

4/24/15/

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EX-OFFICIO MEMBERS
WILLIAM G. McADOO
SECRETARY OF THE TREASURY
CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

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FEDERAL RESERVE BOARD

WASHINGTON

W. P. G. HARDING, GOVERNOR
PAUL M. WARBURG, VICE GOVERNOR
FREDERIC A. DELANO
ADOLPH C. MILLER
CHARLES S. HAMLIN

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

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Dear Sir:-

Under an arrangement recently made, official telegrams of your bank are to be paid for by the Federal Reserve Board at Government rates. Enclosed are certain telegrams, forwarded to the Federal Reserve Board for such payment.

Will you please have these telegrams checked, the count of words in each one verified and return them as early as possible with some certification of an officer of your bank to the effect that they are authentic and should be paid.

Where the Government rate is charged, the address and signature upon telegrams are counted.

Very respectfully,

Fiscal Agent.

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F E D E R A L R E S E R V E B O A R D

WASHINGTON

April 30, 1915.

S I R :-

The question has been raised whether a Federal reserve bank may, under Section 13 of the Federal Reserve Act, discount acceptances endorsed by a member bank located in a district other than that of such reserve bank; and, if so, is the paper thus discounted eligible to be used as collateral security for Federal reserve notes issued under Section 16?

The Act provides that -

> "Any Federal reserve bank may discount acceptances which are based on the importation or exportation of goods and which have a maturity at time of discount of not more than three months, and endorsed by at least one member bank."

It is to be noted that an acceptance to be eligible for discount under this provision of the Act must

(1) be based on the importation or exportation of goods,
(2) have a maturity at time of discount of not more than three months, and
(3) be endorsed by at least one member bank.

The third requirement is the one to be specially considered in this connection. Does "member bank" mean a member of the particular Federal reserve bank, or does it import a more general significance and mean a bank which is a member of the Federal reserve system? If it is the latter, then no doubt any Federal reserve bank may discount acceptances for any member bank, irrespective of the district in which it is located.

Section 1 of the Federal Reserve Act states that -

> "The term "member bank" shall be held to mean any national bank, State bank, or bank or trust company which has become a member of one of the reserve banks created by this Act",

and, applying this definition to the section in question, it would seem clear that in considering the eligibility of acceptances for discount by a particular Federal reserve bank, it is immaterial in what district the endorsing member bank is located. As long as it

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is a member of some one Federal reserve bank, it is a "member bank" as defined by the Act itself.

This conclusion is further supported by the fact that Congress, in defining eligible paper other than acceptances, required specifically that the endorsement must be by "any of its member banks", thus expressly referring to the members of a certain Federal reserve bank. The fact that this restriction was omitted in fixing the qualities of eligible acceptances, indicates that Congress intended that there should be a broad market for this class of paper and that a Federal reserve bank should not be limited to acceptances endorsed by its own member banks,

This same construction of the term "member bank" has been accepted by the Board in relation to the power of a Federal reserve bank to receive deposits of "checks and drafts upon solvent member banks."

Granting, therefore, that a Federal reserve bank may discount acceptances endorsed by a member bank of another district, may such paper be put up as collateral for Federal reserve notes?

It is clear that paper bought in the open market under the provisions of Section 14 is not eligible as collateral security unless it conforms to the provisions of Section 16, defining eligible collateral. That section provides in part that -

> "The collateral security thus offered shall be notes and bills, accepted for rediscount under the provisions of Section 13 of this Act".

If, therefore, a Federal reserve bank receives acceptances for discount under the provisions of Section 13, in the manner indicated above, such paper may be used as collateral for Federal reserve notes. The sole requirement is that the collateral shall be notes and bills, - terms which are broad enough to include acceptances in this connection, - accepted for rediscount under the provisions of Section 13. The fact that the same paper may have been purchased in the open market, with or without the endorsement of a member bank, is immaterial if, in fact, the paper was accepted for discount under Section 13.

As previously indicated, acceptances endorsed by a member bank of another district may be so discounted, and if so,

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they may be put up as collateral security under the terms of Section 16, which define eligible collateral.

Respectfully,

(Signed) M. C. ELLIOTT,

Counsel.

To
Honorable C. S. Hamlin,
Governor, Federal Reserve Board.

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orig by-laws
adopted
Aug. 26, 1914

3/5/15
Print with amends.

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BY-LAWS OF THE FEDERAL RESERVE BOARD

WITH

AMENDMENTS.

By-laws:-

ARTICLE I.

The Chairman.

The Secretary of the Treasury shall be Chairman of the Board, and shall preside at all meetings when present. In the absence of the Chairman the Governor of the Board shall act as presiding officer. In the absence of both the Chairman and the Governor, the Vice Governor shall act as Chairman.

ARTICLE II.

The Governor.

Section 1. The Governor of the Federal Reserve Board shall be the active executive officer thereof; subject, however, to such rules and regulations as may be incorporated herein or may from time to time, by resolution, be established.

Section 2. The Governor shall have custody of such funds as may be in possession of the Board. He shall open and maintain bank accounts in such institutions as the Board may by resolution designate, and shall sign checks drawn on such accounts, such checks to be countersigned by the Secretary or other designated officer of the Board.

Amendments:-

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Section 3. The Governor shall keep or cause to be kept a continuing record of all receipts and disbursements of the Board.

Section 4. The Governor shall have general charge of all business of the Board not specifically assigned by resolution to any individual member thereof, or to the committee of the whole. He shall submit a summary of such business at each succeeding meeting of the Board.

Section 5. The Governor shall have custody of the seal of the Board and shall have power to affix the same to all instruments requiring it under the authority of the Board. Such instruments shall be attested by the Secretary.

ARTICLE III.

The Vice-Governor.

Section 1. In the absence or disability of the Governor, his powers shall be exercised and his duties discharged by the Vice-Governor and in the absence or disability of both of these officers, such powers shall be exercised and such duties discharged by such member of the Board, as it may by resolution, designate Chairman pro tem.

Section 2. It shall be the duty of the Vice-Governor to cooperate with the Governor in the administration of the general business of the Board.

AMENDMENT I.

Section 5 of Article 11 of these By-laws is hereby amended to read:

"The Secretary shall have custody of the seal and shall have power to affix the same to all instruments requiring it under the authority of the Board. Such instruments shall be attested by the Secretary."
(February 1, 1915).

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On motion the amendment to the By-laws of the Board, notice of which had been duly given in accordance with Article 9 of the existing by-laws, was adopted as follows:

Insert after Article III of the existing By-laws, a new article numbered IV, as hereinafter set forth, and renumber the succeeding articles accordingly.

ARTICLE IV.

The Executive Committee.

1. There shall be an Executive Committee of the Board consisting of three members, which shall include the Governor and Vice Governor and one other. The third member shall be nominated and elected at a regular meeting of the Board. Members of the Board shall serve as far as practicable in rotation and for periods to be fixed by the Board from time to time. Two members shall constitute a quorum for the transaction of business.

2. It shall be the duty of the Executive Committee of the Board to transact all business of a general nature which can be transacted in accordance with principles already established by the Board, and such as may be delegated to it from time to time; to review and approve important correspondence involving the expression of opinions or decisions of the Board; to prepare and make recommendations governing the conduct of the Board's business and to oversee and control the making of statements to the press expressive of the Board's policy or descriptive of its action.

3. The Executive Committee may at any time delegate to the Secretary of the Board, either individually or under the supervision of one of its members, the exercise of its functions with reference to publicity as hereinbefore set forth.

(March 22, 1915).

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ARTICLE IV.

Section 1. The Board shall appoint a Secretary, whose duty it shall be to attend all meetings of the Board, and keep a record of its proceedings.

Section 2. The Secretary shall assist the Governor and members of the Board in the administration of general business and correspondence. He shall under the direction of the Governor have general supervision of the office and shall supply the Board with detailed information regarding domestic and international business and banking relations, and such other data as the Board may from time to time require.

Section 3. In the absence or disability of the Secretary, his duties shall be performed by such member of the Board or general staff as said Board, may, by resolution, appoint Secretary pro tem.

Now ARTICLE V.

By Amendment March 22, 1915, above.

AMENDMENT II.

The Board shall appoint an Assistant Secretary, who shall exercise the powers and discharge the duties of the Secretary in his absence or disability and shall perform such other duties as may be assigned to him from time to time by the Board, or by the Secretary of the Board.

AMENDMENT III.

Section 1. The Board shall appoint a Fiscal Agent whose duty it shall be to collect and deposit all moneys receivable by the Board with the Treasurer of the United States, to be placed in a Special Fund established on the books of the Treasury for the Federal Reserve Board.

Section 2. The Fiscal Agent shall execute a bond with surety satisfactory to the Board in a sum to be fixed by the Board.

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Section 3. Payment of expenses and other disbursements of the Board shall be made by the Fiscal Agent, upon proper vouchers, out of the moneys advanced to him by requisition and warrant out of the Special Fund and placed to his official credit with the Treasurer of the United States, as provided by Section 5 of this amendment.

Section 4. The Fiscal Agent shall prepare a monthly account in such form as shall be approved by the Comptroller of the Treasury, and, after approval by the Governor, such monthly account shall be submitted to the Auditor for the State and other Departments.

Section 5. The Governor shall, when necessary make requisition on the Treasurer of the United States for the advance of such sums to the Fiscal Agent as may be necessary from the Federal Reserve Board Fund.

AMENDMENT IV.

So much of the provisions of the By-laws heretofore adopted inconsistent with Amendments I, II and III are hereby repealed.
(February 1, 1915.)

Now ARTICLE VI.

By Amendment March 22, 1915, above.

ARTICLE V.

The following is an impression of the seal adopted by the Board:

(SEAL)

ARTICLE V- a.

Counsel.

The Board shall appoint a regular Counsel whose duty it shall be to advise with the Board, or any mem-

Now ARTICLE VI- a.

By Amendment March 22, 1915, above.

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ber thereof, as to such legal questions as may arise in the conduct of its business; and to prepare, at the Board's request, forms and other legal papers and to perform generally such legal services as he may be called upon by the Board to perform.

ARTICLE VI.

Meetings.

Section 1. There shall be a stated meeting of the Board each week day except Saturdays and legal holidays at 11 a.m.

Section 2. A majority of the Board shall constitute a quorum for the transaction of business except that an affirmative vote of at least five members of the Board shall be necessary to require Federal reserve banks to rediscount the discounted paper of other Federal reserve banks.

Section 3. At least once during each quarter there shall be a joint conference in Washington of members of the Federal Reserve Board and the Federal Reserve Advisory Council, at such time as may be mutually agreed upon by said Board and said Council.

Section 4. At all meetings of the Board the following shall be the order of business:

(1) Reading or inspection of the minutes of the last regular meeting.
(2) Report of the Governor.
(3) Report of the Secretary.
(4) Reports of the committees or members on assigned business.
(5) Unfinished business.

Now ARTICLE VII.

By Amendment March 22, 1915, above.

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ARTICLE VII.

Information.

Section 1. All persons employed by the Board shall keep inviolate its business, affairs, and concerns, and shall not disclose or divulge the same to any unauthorized person whomsoever, and any employee who shall give information contrary to this by-law shall be liable to immediate dismissal.

Section 2. Unless a different procedure in given cases is authorized by vote of the Board, the action or policy of the Board shall not be expressed through any individual member, but by its duly constituted officers, after formal action by the Board.

Now ARTICLE VIII.

By Amendment March 22, 1915, above.

ARTICLE VIII.

Committee on Budget and Audit.

The Chairman shall appoint a committee consisting of two members of the Board, whose duty it shall be to audit the accounts thereof for the six months' period for which they shall have been appointed, and report to the Board a tentative budget of expenses for the next succeeding six months.

Now ARTICLE IX.

By Amendment March 22, 1915, above.

ARTICLE IX.

Amendments.

These by-laws may be amended at any regular meeting of the Board by a majority vote of the entire Board, provided that a copy of such amendment shall have been delivered to each member at least seven days prior to such meeting.

Now ARTICLE X.

By Amendment March 22, 1915, above.

5/5/15.

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STATEMENT FOR THE PRESS:

May 4, 1915.

The Federal Reserve Board today passed the following resolution regarding redistricting appeals:

BE IT RESOLVED: That the recommendations of the respective committees be adopted and approved, and that the petitions of the banks in southern Oklahoma, northern New Jersey, Tyler and Wetzel Counties, West Virginia, be granted; and,

BE IT ALSO RESOLVED, That the petition of the banks of Wyoming and Nebraska be denied; and,

BE IT FURTHER RESOLVED, That action on other pending petitions be deferred until further experience in the actual operation of the several districts, especially in the light of the new clearing system which is about to go into effect, and of the extent to which State banks take membership in the Federal Reserve System, shall have provided the Board with the necessary data for a conclusion, it being the opinion of the Board that action on petitions relating to changes in cities designated as the location of Federal Reserve banks should be deferred until the Board shall have reached a conclusion from experience as to any further readjustments in the boundaries of the several districts, or in the number of districts, which may be desirable in the operation and development of the Federal Reserve System.

The vote on the resolution was unanimous, Secretary McAdoo who was not present, asking to be recorded in favor of it .

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Federal Reserve Bank of St. Louis

FEDERAL RESERVE BOARD

WASHINGTON

May 6, 1915.

MEMORANDUM IN REGARD TO CENTRAL RESERVE AND RESERVE CITIES.

Attached hereto (Exhibit A) is a list of Central Reserve and Reserve Cities, grouped according to the Federal Reserve Districts in which they are located and showing the population of each. It is apparent without much study, that no very intelligent method has thus far been practiced in the selection of these cities. New York City is the only Central Reserve City in the Eastern states and Chicago and St. Louis, quite close together, represent all the rest of the country.

Some important Federal Reserve Districts have only one Reserve City; for example, Boston and Philadelphia. Three of the Districts have only two Reserve Cities, New York, St. Louis, and Minneapolis. In the case of Minneapolis, the other Reserve City is St. Paul, although, in relation to trade and commerce, Minneapolis and St. Paul are twins.

Some of the Reserve Districts are amply supplied with Reserve Cities and one or two have gone to almost absurd extremes in this respect.

It would, therefore, seem that there should be a reconsideration of the whole subject. With this object in view and for the information of the Board there is attached hereto (Exhibit B) a list showing all cities of over 100,000 in-

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habitants, fifty in all, and all cities of less than 100,000, but over 50,000, fifty-four cities.

These Exhibits illustrate better than argument the reasons for a reconsideration of the whole subject of the selection of Reserve and Central Reserve Cities.

Under the Act until November 2nd, 1917, all non-reserve city banks may keep five-twelfths (5/12) of their reserve deposits in other national banks in Reserve or Central Reserve Cities,

Secondly; minimum reserve requirements are fixed for all time at 18% for banks in Central Reserve, 15% for banks in Reserve and 12% for banks in non-reserve cities.

Third; the law specifically permits the Federal Reserve Board to readjust the matter of Reserve or Central Reserve Cities at any time so that if at the end of the three-year period, (i. e. November 2nd, 1917) it were thought desirable to reduce or rearrange the list of Reserve and Central Reserve Cities, it could be readily done. Incidentally it may be said that there is much to be said in favor of higher reserve requirements in large cities, say cities of half a million or more inhabitants where, by reason of congested population, or similar causes, there may be sudden demands for funds.

The question of naming additional Reserve Cities or Central Reserve Cities naturally divides itself into two

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parts; first, the effect in the next two and a half years, and, second, the effect thereafter. At the same time, inasmuch as the Federal Reserve Board has the right on November 2nd, 1917, or at any subsequent date to readjust this whole schedule of Reserve and Central Reserve Cities, one need not be alarmed by the effect at that time, and we may therefore confine our attention to the immediate results. Taking the case of Central Reserve Cities first, we may state that the immediate results are threefold:

> First; An increase in reserve requirements of all National banks in Central Reserve Cities from 15% to 18%;
>
> Second; As a compensation for this, all Reserve Cities are permitted to count as part of their reserves, deposits in banks in Central Reserve Cities;
>
> Third; Perhaps of most immediate importance, is the fact that banks in Central Reserve Cities must keep all their reserve deposits either in their own vaults or in their Federal Reserve Bank, thus greatly strengthening it.

If, for example, we were to name the cities of Boston, Philadelphia, Cleveland, Minneapolis, Kansas City and San Francisco as Central Reserve Cities, the immediate effect would be:

> To increase the reserve requirements of banks in those cities 3%;
>
> To permit Reserve Cities to count as part of their reserves, deposits in banks in those cities;
>
> To strengthen the Federal Reserve Bank of each respective district by increasing it deposits.

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Taking the concrete examples of Boston, Philadelphia, Clevaland, Kansas City, Minneapolis and San Francisco, it might be argued that these cities should not be named as Central Reserve Cities unless important cities and towns in these districts are named as Reserve Cities. Thus in the Boston district we might properly name Portland, Me., Providence, R.I., Hartford and New Haven, Conn.

We might add to the Reserve Cities in the New York district Buffalo and Syracuse.

We might add to the Reserve Cities of the Philadelphia district Harrisburg and Scranton, Pa.

We might add to the Reserve Cities of the Cleveland district Dayton and Toledo, Ohio.

There does not seem to be any necessity of adding any Reserve Cities in the San Francisco district, as there are already six Reserve Cities in that district, outside of San Francisco.

We might add to the St. Louis district Memphis, Tenn., and Little Rock, Ark., and to the Minneapolis district Duluth, Minn and possibly Butte, Montana.

The above tentative suggestions for abvious reasons omit any reference to Central Reserve Cities in the Districts of Richmond, Atlanta and Dallas.

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EXHIBIT "A"

List of Central Reserve and Reserve Cities, Grouped by Districts and According to Population.

DISTRICT NO. 1:

	Population
(*) Boston	670,585

DISTRICT NO. 2:

(*) New York City	4,766,883
Albany	100,253

DISTRICT NO. 3:

(*) Philadelphia	1,549,008

DISTRICT NO. 4:

(*) Cleveland	560,663
Pittsburgh	533,905
Cincinnati	364,463
Columbus	181,548

DISTRICT NO. 5:

Baltimore	558,485
Washington	331,069
(*) Richmond	127,628
Charleston S.C.	58,883

DISTRICT NO. 6:

New Orleans	339,075
(*) Atlanta	154,389
Birmingham	132,685
Nashville	110,364
Savannah	65,064
Chattanooga	44,604

DISTRICT NO. 7:

(*) Chicago	2,185,283
Detroit	465,766
Milwaukee	373,857
Indianapolis	233,650
Des Moines	86,368
Sioux City, Ia.	47,828
Dubuque	38,494
Cedar Rapids	32,811

DISTRICT NO. 8:

(*) St. Louis	687,029
Louisville	223,928

DISTRICT NO. 9:

	Population.
(*) Minneapolis	301,408
St. Paul	214,744

DISTRICT NO. 10:

(*) Kansas City, Mo.	248,381
Kansas City, Kas.	82,331
Denver	213,381
Omaha	124,096
South Omaha, Neb.	26,259
St. Joseph, Mo.	77,403
Oklahoma City	64,205
Wichita, Kas.	52,450
Pueblo, Colo.	44,395
Lincoln, Nebr.	43,973
Topeka, Kas.	43,684
Muskogee, Okla.	25,278

DISTRICT NO. 11:

San Antonio	96,614
(*) Dallas	92,104
Houston	78,800
Ft. Worth	73,312
Galveston	36,981
Waco	26,425

DISTRICT NO. 12:

(*) San Francisco	416,912
Los Angeles	319,198
Seattle	237,194
Portland	207,214
Spokane	104,402
Salt Lake City	92,777
Tacoma	82,972

Federal Reserve Cities marked with (*)

Apr. 23, 19[illegible]

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F E D E R A L R E S E R V E B O A R D

WASHINGTON.

May 8, 1915.

GOLD SETTLEMENT FUND.

Instructions to Federal Reserve Banks relative to the establishment of the Gold Settlement Fund.

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1 - At close of business Wednesday, May 19, 1915, each Federal reserve bank will telegraph to the Federal Reserve Board the amounts in even thousands due to each other Federal reserve bank as of that date.

2 - Thursday, May 20, Settling Agent will telegraph to each bank the amounts of credits to its settlement account, giving the name of each bank from which such credits were received, also net debit or credit balance in settlement. A confirmation will be sent by mail.

3 - Each bank will be expected to forward to the nearest subtreasury not later than Monday, May 24, 1915, in gold, gold certificates or gold order certificates properly endorsed, at least $1,000,000, and in addition an amount equal to its net debit balance as telegraphed by the Settling Agent. Transfers of gold or gold certificates should be credited to the account of "Gold bullion and U. S. coin" and "U. S. gold certificates" and charged to the item "Gold Settlement Fund" on the books of the Federal reserve banks.

4 - As soon as all transfers have been effected, each Federal reserve bank will be advised by telegraph at which time the transfer entries should be made on the books of the bank. Each Federal reserve bank will then debit the due to Federal reserve banks' accounts and credit the Settlement Fund and will credit the due from Federal reserve banks' accounts and charge the Settlement Fund.

5 - The second settlement will be made on May 27 and figures telegraphed as at close of business on May 26, and at weekly intervals thereafter.

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