

July 24, 1915.

MEMORANDUM ON THE RIGHT OF THE FEDERAL RESERVE BOARD TO RESTRICT THE REDISCOUNT BY FEDERAL RESERVE BANKS OF ACCEPTANCES BASED ON THE EXPORT OF MUNITIONS OF WAR.

The question has been raised whether the Federal Reserve Board has the right, under the power to regulate, to restrict the rediscount by Federal Reserve Banks of acceptances based on the export of war materials.

Section 13 of the Federal Reserve 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 the time of discount of not more than three months, and indorsed by at least one member bank."

It is evident that an acceptance to be eligible for rediscount under the provision herein quoted must be based on the importation or exportation of goods. Congress, however, in defining this power of the Federal Reserve Banks, has made no restriction whatever on the character or quality of the goods exported. The sole limitation in this connection is that the acceptance be based on the importation or exportation of goods, and, if it covers such a transaction, it may, under the terms of the Act, be rediscounted by the Federal Reserve Bank irrespective of the kind, quality, or ultimate use of the goods so exported or imported, provided, of course, that the acceptance also possesses the requisite indorsement and maturity.

It is also provided in Section 13 that "The rediscount by any Federal Reserve Bank of any bills receivable and of domestic and foreign bills of exchange, and of acceptances authorized by this Act, shall be subject to such restrictions, limitations, and regulations as may be imposed by the Federal Reserve Board", and it might be argued, therefore, that the Board has the right under this provision to issue a regulation to the effect that only those acceptances which are based on the export of non-contraband goods shall be eligible for rediscount. Such a regulation, even if intended by Congress, would be unconstitutional as a legislative act.

Many cases of the United States Supreme Court have clearly settled the principle that the power of an administrative body, such as the Board, to regulate or to impose restrictions or limitations on those rights or powers authorized by an Act of Congress is limited to the mere administration of such Act, to

the making of regulations which will make the will of Congress operative and effective. Any regulation which either unduly restricts or enlarges the powers or privileges conferred by Congress is void and of no effect, because an unconstitutional exercise of a purely legislative function.

Congress has specifically authorized the discount of acceptances based on the exportation or importation of goods. If the Board should pass a regulation requiring that such banks should discount only acceptances based on the exportation of non-contraband goods, it would seem that it would thereby improperly restrict the authority given by Congress itself. If it were legitimate to make such a regulation, the logical consequences would be that the Board could, if it saw fit, regulate that acceptances based on the export of goods other than vegetable products should not be discounted, or that acceptances based on the export of goods other than works of art should not be discounted; or, *reductio ad absurdum*, that acceptances based on the export of goods other than peanuts should not be rediscounted. Such a power, if conceded, would enable the Board under the guise of administration, completely to nullify the provisions of the Act, and its exercise would be clearly unconstitutional.

It is to be noted incidentally that if the Board has the right, under the power to regulate, to restrict the discount of acceptances as previously indicated, it may also similarly limit the discount of commercial paper to paper the proceeds of which are to be used, for instance, for certain limited agricultural pursuits.

What then does this power to regulate involve? As indicated by the cases decided in the Supreme Court, the power to regulate confers on the body possessing it the right to make any regulation which will conduce to the effective operation and administration of the law as passed by Congress. Any regulation, however, which not only fails to promote an effective administration of that law, but rather tends to nullify it in whole or in part, is not such a regulation as may be legitimately promulgated by any administrative body of the government.

It seems, therefore, that the Board can not restrict the rediscount of acceptances to those acceptances which are based on any particular class of goods, or to acceptances based on goods being transported to any particular place or country. Such a regulation would be a discrimination clearly not contemplated by Congress, and one which might well provoke just criticism of the Board.

There seems to be no doubt, however, that the power of the Board to regulate the discount of acceptances confers upon it not only the power but also the duty to make certain restrictions, such as upon the total amount of acceptances rediscounted by any particular bank or banks, if it is seen at any particular time that the assets of any such bank or banks should be conserved for other more urgent needs. The whole purpose of the Act demands that the Board possess such regulatory power in order to make effective the machinery provided by the Act for affording means of moving crops, for instance, or for preventing financial panics.

Such a general power, however, has no relation to, and does not include the right to exclude a particular class of paper which could not be classified separately on any ground of financial policy, or for any reason except perhaps to satisfy the complaints of certain persons inspired only by their own personal or emotional prejudices.

In any event, it is very certain that under the present regulations of the Board, any Federal Reserve Bank may discount acceptances based on the exportation of goods, whether war materials or not, and it does not seem, for the reasons indicated, that the Board can legally issue a new regulation which would impose any restriction operating as a discrimination against any particular class of goods such as war materials.

Attention is respectfully directed to Mr. Elliott's opinion, filed with the Board, which deals more generally with the broader question of the status of the Federal Reserve Banks, and with the question of the neutrality of the United States government in this matter.

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