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PRESS STATEMENT.

January 13, 1917.

After having given much attention to the problem of controlling and regulating the gold supply of the United States and to the question of bank reserves in general, the Federal Reserve Board has prepared and transmitted to the Chairmen of the Committees on Banking and Currency of the Senate and House of Representatives recommendations for the amendment of the Federal Reserve Act. While it is not deemed desirable to give out the text of the amendments transmitted, since they will probably soon be introduced in Congress, the following general statement concerning them is made public.

When the Federal Reserve Act was drafted its principal object was to deal with national problems of banking and currency. Since its enactment financial and economic conditions in the United States have undergone far-reaching changes which were not foreseen three years ago. The United States has grown to be a world power in financial affairs and it seems necessary that the Act, which has proved of such great value in the treatment of our domestic problems, should now be amended in order to enable us to deal effectively with the new international problems which seem destined to play so important a part in our economic life. The banking system of the United States should be prepared to meet effectively two conditions of opposite character - one, the excessive and uncontrolled inflow of gold, the other the excessive and unregulated outflow of gold. The amendments proposed are designed to provide means of controlling an over-extension of loans based on new accretions to our gold stock and to provide for the mobilization and concentration of the gold holdings of the United States so that the flow of gold back into Europe, or to South America or to the Orient, may be arranged without forcing any violent contraction of loans or causing undue disturbance to legitimate business.

Of approximately two and three-quarter billions of gold in this country there are held or controlled by Federal reserve banks about \$736,000,000, of which Federal reserve agents hold \$283,000,000 as security for Federal reserve notes outstanding, and \$453,000,000 is reserve money and must therefore be used conservatively. But even assuming that the Federal reserve banks were willing to reduce their gold reserves to 40% of their deposits and note liability

-2--

(which would be regarded as a minimum and in normal times would be inadequate) the amount of free gold, i. e., the amount of gold that the Federal reserve banks would lose before reaching this 40% minimum, would be a little more than \$375,000,000. While this is a very large sum its sufficiency can not safely be assumed when we consider the wide scope of our transactions in world finance and the phenomenal growth of our own credit structure.

It is estimated that there are now in the hands of the public, i. e., outside the Treasury and the banks, over eight hundred million dollars in gold and gold certificates, and that there are at present held in the vaults of member banks about \$815,000,000 of reserve money of which \$540,000,000 is gold coin or gold certificates. There should be added to this estimate about \$600,000,000 of lawful money in the vaults of nonmember State banks and trust companies.

NOTE AMENDMENT.

The Federal reserve note, which is an obligation of the United States secured by an ample reserve of gold and commercial paper, is accepted as willingly by the public as a national bank note or as any other form of currency, and the public does not discriminate between different forms of United States currency. Federal reserve note circulation has been substituted for gold certificates to the extent of about three hundred million dollars.

Under the present law this gold is deposited with the Federal reserve agents in redemption of the Federal reserve notes issued against it. The note so provided for thereby in effect ceases to be an obligation of the Federal reserve bank; but as the gold does not figure as an asset of the Federal reserve banks, the Federal reserve banks are unable to show the greater strength which might be evidenced if the law permitted, as proposed in the amendments, the issuance of Federal reserve notes not only against commercial paper, but also against gold or against either, provided always that every Federal reserve note must be covered by at least 100% of commercial paper or gold, and that there must always be a gold reserve of not less than 40% against all outstanding Federal reserve notes.

RESERVES.

The control of gold by Federal reserve banks in times of abundance such as at present, will decrease the danger of inflation of domestic credits and at the same time will enable the country when the tide turns to part with large sums of gold with less inconvenience or shock, thus enabling us more safely and effectively

-3-

to proceed with the development of our foreign trade and to give the necessary credit facilities for its extension. The United States should be in a position to face conditions which may call for an outflow of gold without any disturbances of our own or to the world's business, and without making necessary drastic changes in our interest or discount rates. The amendments suggested by the Board are designed to enable the Federal reserve banks to withdraw gold from actual circulation while enabling member banks at the same time to release gold which at present is tied up in their own vaults. The amendments are based upon the theory that all of the individual banks should strengthen the gold holdings of the Federal reserve banks. The country's holdings of gold are not used most effectively when they are in the vaults of a large number of banks scattered all over the country, but its greatest use would come from concentrating it to a greater degree in the vaults of the Federal reserve banks, where it can be effectively protected when not required and effectively used when needed. The member bank does not require gold with which to supply the ordinary demands of its depositors so much as currency.

It is from this point of view that the Federal Reserve Board has proposed that Congress increase the required reserves to be maintained by member banks with the Federal reserve banks. On November 17, 1916, the cash holdings of all member banks were about \$815,000,000. Under the proposed amendment of Section 19, \$250,000,000 of this amount would be transferred to the Federal reserve banks. Hence the Board believes that ultimately the law should require of member banks no more than that they should maintain a specified balances with the Federal reserve banks in amounts adequate to supply the necessary reserve basis, and that the Federal reserve banks must have sufficient reserves of gold with which to protect all obligations, but that there should, however, be no legal requirement as to the amount of currency that a member bank should carry in its own vault. This is a matter of business judgment that might well be left to the discretion of each member bank. It was thought, however, that if this principle were carried into full effect at this time, the step might be considered too extreme, particularly under present conditions, and nothing should be done that might tend to a further release of reserve money.

A minimum amount of currency that the member banks should be required to keep in their vaults is, therefore, prescribed. The amount suggested is 5% of the demand deposits, so that the total requirements - cash and reserve - will remain practically unchanged. While the effect of some of the proposed

-4-

changes will be to reduce somewhat the reserve requirements, the reserves will be increased by the abrogation of the practice hitherto observed of counting items in transit or "float" as reserve. The permission given member banks to use their own discretion as to the character of currency in their vaults, will enable them to release the gold they now hold, with the important result that the substitution of Federal reserve notes for gold and gold certificates will be facilitated by this change in the law. Without some such change member banks will continue to ask for gold certificates in small denominations, because as long as they must have gold or lawful money to count as reserve it would be impossible for the banks to exchange them for Federal reserve notes.

OTHER PROPOSED AMENDMENTS.

Besides the proposed changes relating to note issues and to reserves the Board has suggested also the following:

Amendment of section 11 so as to permit the Federal Reserve Board to raise reserve requirements in emergencies, just as it is now empowered in certain contingencies of a different kind to lower those requirements.

This provision would, if adopted, enable the Federal Reserve Board in prolonged periods of extreme ease in the money market to check any tendency toward excessive loans or other forms of undue extensions of credit.

Amendment of Section 16 to permit nonmember State banks and trust companies, even though too small to be eligible for membership in the Federal reserve banks, to avail themselves of the clearing and collection facilities of the Federal reserve banks, provided that they cover at par checks on themselves sent for collection by the Federal reserve bank, and provided further that they keep a compensating balance with the Federal reserve bank in an amount to be determined under rules prescribed by the Federal Reserve Board. This is not intended to operate as an extension of any of the privileges of the Federal reserve system to nonmember banks at the expense of members, but on the contrary the amendment is proposed primarily for the convenience of the public and incidentally for the benefit of the member banks. It is contemplated that the compensating balances which nonmember banks participating in the clearing plan will be required to keep with Federal reserve banks, will be sufficiently large to protect member banks and justify Federal reserve banks in undertaking the service. Any clear-

-5-

ing and collection plan to be effective must be so comprehensive as to include all checks. At present the par lists of the Federal reserve banks include the names of banks checks on which can be collected in any circumstances at a minimum of time and expense, but do not embrace a large number of towns in every State where there are no member banks; and in order to make collections on such points many banks are obliged to maintain accounts in addition to their reserve accounts with the Federal reserve banks. A necessary factor in any successful clearing plan is the offset, whereby balances only require settlement instead of the total volume of transactions. As long as the clearing system does not embrace all of the banks this offset is lost in a corresponding degree and the value of the system diminished in proportion.

Amendment of Section 22 - the penal statute - so as to define more clearly the rights and limitations of directors in the matter of accepting fees or compensation other than the ordinary fees paid directors for legitimate services rendered in the regular course of business, the performance of which service is not incumbent upon them in their capacity as directors.

Amendment of Section 13 to restore the provision which was by error stricken from the Act in the amendments of September 7, 1916, thus restoring to national banks, with the approval of the Federal Reserve Board, the right to accept up to 100% of their capital and surplus in transactions involving imports or exports.

Amendment of Section 17 to cancel the provision of the National Bank Act which requires national banks to maintain a minimum deposit of Government bonds with the Treasurer of the United States. National banks are no longer required to keep outstanding a minimum amount of circulating notes, and a newly organized bank is not obliged to purchase or carry any bonds of the United States; but there are a number of national banks organized before the passage of the Federal Reserve Act which have retired their national bank circulation in full, yet they are, under a construction of the old law, required to keep on deposit with the Treasurer of the United States, a certain minimum of United States bonds. The Board feels that it is just to these banks that they be relieved of this obligation.

Amendment of section 25 to authorize member banks located in cities of more than 100,000 population and which have

a capital and surplus of more than \$1,000,000 to establish branches in the same city, provided the State laws do not prohibit State banks and trust companies from establishing branches.

Amendment of Section 9 to authorize mutual savings banks not having capital stock to become associate members of the Federal reserve system under certain prescribed conditions. The principal beneficiaries of this amendment would be the mutual savings banks of the eastern and New England States, which can not become members of the Federal reserve system under the present law owing to the lack of any provision enabling them to subscribe for capital stock of a Federal reserve bank, as they have no capitalization of their own upon which a percentage could be based. They would be required to carry a reserve balance with the Federal reserve bank against their time deposits in the same proportion as member banks; and the accommodations proposed for mutual savings banks are limited strictly to the discount of their thirty-day obligations properly secured.

Amendment of Section 18 so as to give to United States one-year 3% gold notes in the hands of Federal reserve banks the circulation privilege for the issuance of Federal reserve bank notes, such circulation to be taxed at the same rate as circulating notes, which are secured by 3% bonds of the United States. In the opinion of the Board it is desirable to extend this privilege to the Federal reserve banks in order that they may have additional means of protecting themselves at times when there is an unusual demand for currency.

Amendment of Section 4 to abolish the title and office of deputy Federal reserve agent, thus having two unattached Class "C" directors instead of one as at present, and to create the position of assistant Federal reserve agent, who shall not be a director of the bank, but who shall be a salaried bonded officer in the Federal reserve agent's department, serving at all times as an assistant to the Federal reserve agent and qualified to act for the agent in his absence. Experience has shown that there is difficulty in filling the office of deputy Federal reserve agent. This officer is required to have the same qualifications as the Federal reserve agent; he must have had banking experience and he must not be an officer, director, or stockholder in any bank. At the same time he is not as a rule a salaried officer, and receives only the customary fees paid directors for attendance upon meetings, and he is obliged to be prepared to assume the duties of the Federal reserve agent in case of the absence or disability of that officer, which involves a transfer and audit of securities and accounts. It is believed that the change suggested will operate to fix responsibility more definitely and will give the Board more latitude in the selection of the Class "C" directors other than the Federal reserve agent.