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

FEDERAL RESERVE BOARD

WASHINGTON

CHARLES S. HAMLIN, GOVERNOR
FREDERIC A. DELANO, VICE GOVERNOR
PAUL M. WARBURG
W. P. G. HARDING
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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

At the beginning of my service on the Federal Reserve Board I had a rather strong feeling, which perhaps amounted to a prejudice, that Federal Reserve notes should not be counted as reserve by National banks. During the twenty-two months of my service I have given the matter careful thought and study and while my mind is perhaps not fully made up, and certainly still open to conviction, I have rather come to the conclusion that my first view was a mistake and that there is at least a good deal to be said on the other side.

I have attempted to state the case fully and fairly in the attached memorandum and I should be very glad to have you read it at your convenience and give me the benefit of your suggestions and criticisms. Please understand that this memorandum expresses only my personal views and expressions.

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1373

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

701

June 16, 1916.

Dear Sir :

There is enclosed for your information and attention copy of a resolution adopted by the Federal Reserve Board at a meeting held on June 16, levying an assessment of seventy-five thousandths of one per cent (.00075) against Federal Reserve Banks to defray the estimated general expenses of the Federal Reserve Board from July 1 to December 31, 1916. This assessment does not include the cost of engraving and printing Federal Reserve notes.

There is also enclosed a statement showing the basis upon which the assessment is levied.

I have the honor to request that you bring this mattter to the early attention of the Board of Directors of your bank, and forward the assessment to the Federal Reserve Board, one-half to be payable July 1st and one-half on September 1st, 1916, as indicated in the resolution.

Very truly yours,

Fiscal Agent.

Enclosures.

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SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

766

Dear Sir:

The Federal Reserve Board has given careful consideration to the letters received from the various Federal reserve banks in response to a letter sent out by Mr. McKay regarding the issuance of par lists in connection with the clearing system to be inaugurated July 15th.

In order to meet as nearly as possible the wishes of all, it has been decided for the present to print a par list showing each State separately along the lines of the enclosed specimen sheet.

The majority of the banks having advised their inability to furnish before July 15th a list of non-member banks on which items will be received at par, the printing of the lists will necessarily be delayed, but it is desired that the preliminary list be issued in time for distribution before August 1st.

You are, therefore, requested to furnish in duplicate a list of the State member banks and non-member banks in your district upon which items can be handled by you at par, this list to be in the hands of the Board by July 23rd. It is intended to distribute the complete list by August 1st, as well as to include it in the August Bulletin.

You are also requested to send in to the Federal Reserve Board, so as to be received before the 23rd of each month, a list showing all additions and reductions in the list of non-member banks upon which items can be handled by you at par. These lists when received will be consolidated, and each Federal reserve bank will be advised of all changes, so that the information can be transmitted to its member banks. It is also intended to show the list of changes in the monthly Bulletin.

Very truly yours,

Governor.

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

W A S H I N G T O N

To all Federal Reserve Agents:

The prohibitions of Section 8 of the Clayton Act which relate to interlocking bank directorates go into effect on October 15, 1916. These prohibitions relate to banks organized or operating under the laws of the United States, and, therefore, apply to State banks or trust companies which are members of the Federal Reserve System as well as to national banks. For convenience, therefore, banks "organized or operating under the laws of the United States" will be referred to as "member banks."

ANALYSIS OF SECTION 8 OF THE ACT

As originally enacted, Section 8 of the Clayton Act provides, in substance -

(a) That no person shall be a director, officer or employee of a member bank having resources aggregating more than $5,000,000 and at the same time a director, officer, or employee of any other member bank;

(b) That no private banker or person who is a director of a non-member bank having resources aggregating more than $5,000,000 shall be eligible to serve at the same time as a director in any member bank;

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(c) That no member bank in a city of more than 200,000 inhabitants 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 or trust company located in the same place.

EXCEPTIONS.

The provisions of Section 8:

(1) Do not apply to mutual savings banks not having a capital stock represented by shares.

(2) Do not prohibit a person from being at the same time (a) a Class "A" director of a Federal reserve bank and also an officer or director, or both an officer and a director, in one member bank; (b) an officer, director or employee of one member bank and one other bank or trust company, whether a member bank or non-member bank, where the entire capital stock of one is owned by the stockholders of the other.

THE KERN AMENDMENT

By an Act of Congress, approved May 15, 1916, Section 8 was amended by the addition of a further proviso reading as follows:

> "Nothing in this Act shall prohibit any officer, director, or employee of any member bank, or Class "A" director of a Federal reserve bank, who shall first procure the consent of the Federal Reserve Board * * * * * from being an officer, director, or employee of not more than two other banks * * * * * if such other bank * * * * is not in substantial competition with such member bank."

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The duty imposed upon the Federal Reserve Board in passing upon any application made under authority of this amendment is to determine whether or not the two banks in question (or either of them) are in substantial competition with the member bank. If both are non-member banks the act does not require that they shall not be in substantial competition with each other.

In reaching a conclusion on this point, it will be necessary for the Board to call upon the Federal Reserve Agent, as its local representative, to make investigation of the facts in each case, to report the same to the Board and to give the Board the benefit of his recommendation whether the consent applied for shall be granted or refused. It is, therefore, necessary to call to the attention of the Federal reserve agents some of the factors which must be considered in determining the question of whether or not the banks involved are in substantial competition.

PURPOSES OF THE ACT AND THE AMENDMENT.

The significance of the language "substantial competition" can not be fully understood without considering the purpose of the original act as well as that of the amendment.

As outlined by the Judiciary Committee, in reporting the original bill to the House, the purpose of Section 8, of the original Clayton Act was -

> "to prevent as far as possible control of great aggregations of money and capital through the medium of common directors between banks and banking associations, the object being to prevent the concentration

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of money or its distribution through a system of interlocking directorates."

It will be observed that the Act does not undertake to prevent interlocking directorates of banks located in small cities and having small aggregate resources. It applies in terms to the qualification of directors, officers and employees of banks (a) in cities of more than 200,000 inhabitants or (b) having resources aggregating more than $5,000,000.

While the general purpose of the Act, as indicated by its title, was "to supplement existing laws against unlawful restraints and monopolies," and while monopolies are created by a restraint of legitimate competition a literal interpretation of Section 8 as originally enacted would prohibit a person from serving at the same time as a director, officer or employee of two or more banks, under certain circumstances, whether or not such banks were competitors. The Kern amendment, however, authorizes the Board to permit a director, officer or employee of a member bank who otherwise would be ineligible, to serve as a director, officer or employee of not more than two other banks or trust companies, whether State or national, provided such other banks or trust companies are not in substantial competition with such member bank.

It should be borne in mind that the Act does not vest an arbitrary discretion in the Board to permit the same person to serve on the board of directors of any two or more banks, when such banks come within the restrictive language of the Act as

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originally passed; but it merely confers authority upon the Board to permit interlocking directorates when such banks are not in substantial competition, within the meaning of the Act.

SUBSTANTIAL COMPETITION.

It is manifest that no fixed rule can be prescribed by which this question can be automatically determined. The facts in each case must be carefully considered and it is the duty of the Board to withhold its consent in any case in which it would defeat the purposes of the Act to permit the same person to serve as an officer, director, or employee of more than one bank.

If the two banks in question are not competitors in any respect no question arises. If they do compete the very difficult question arises, whether or not the competition is "substantial".

It is necessary to keep in mind that the main purpose of the Act was to prevent the monopolization and centralization of credit through interlocking directorates of banking institutions. One of the injurious results of such conditions is that the public is deprived of the benefit of legitimate competition.

In general, therefore, two banks coming within the prohibition of the original Act would be deemed to be in substantial competition within the meaning of the language used in the amendment if the business engaged in by such banks under

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natural and normal conditions, conflicts or interferes, or if the cessation of competition between the two would be injurious to customers, or would-be customers, or would probably result in appreciably lessening the volume of business or kinds of business of either institution.

It is realized that some difficulty will be experienced in the application of this test.

Two banks engaged in the same character of business (for example, where both receive commercial deposits and make commercial loans) would be regarded as in substantial competition if their fields of activity extended over the same geographical territory. If their operations were not carried on in the same geographical territory, then, although they engaged in the same class of business, they would not necessarily be regarded as substantial competitors.

Again, if they conducted their operations in the same place, but, because of their comparatively small size in relation to the total banking opportunities of the locality, and because of the fact that they did not deal with the same class of customers, the cessation of competition between them might, from the public point of view, be unimportant, they would not necessarily be deemed to be in substantial competition. Or, if their operations were conducted in the same locality but the character of business engaged in differs (for example, where one does a strictly commercial banking business while the other confines its operations

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to a trust company or fiduciary business), such banks need not be regarded as in substantial competition.

It is, therefore, necessary to consider the scope or extent of territory that a bank's operations cover and the character and kinds of business it engages in. Size, measured by aggregate resources, will constitute one of the factors to be considered, since to increase the volume of loanable funds usually increases the radius of a bank's operations. A bank with $100,000,000 resources would seek investments in a larger area and of a more diverse character than a bank with $5,000,000, and so might come into competition with banks located some distance away, while the bank with $5,000,000 resources might not extend its activities to any real extent beyond the borders of the city in which it is located. For example, a bank in New York might come into substantial competition with a bank in Chicago if both were engaged in the same class of business and if both had become so large as to be more than local institutions.

Where the operations of the two banks cover a common territory from a geographical standpoint, it is necessary to consider carefully the character of business engaged in. As a very large proportion of the member banks do a commercial banking business, the volume of this business within the territory covered by the operations of the banks in question becomes an important factor. In a city of 250,000 inhabitants any two banks which engaged in a

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commercial banking business to any great extent would presumably come into substantial competition, whereas, in a city of 2,000,000 inhabitants one bank might confine its operations to the wholesale district while another might draw its customers exclusively from the retail district, and so might be non-competitive in the sense that an increase of the business of one would not affect the business of the other.

R E S U M E'

It is, therefore, necessary that consideration should be given:-

(1) To the size in aggregate resources of banks involved;

(2) To the character of business engaged in, i. e., the extent of commercial business and extent of purely investment or trust company business of the two institutions.

(3) Whether the operations of the two banks cover the same geographical territory.

(4) Whether the two banks actually compete to any appreciable extent in any important activity - for example, (a) in soliciting deposits on demand or on time from other banks or individuals, (b) in the purchase or sale of commercial paper or other securities, (c) in the purchase or sale of foreign exchange, (d) in soliciting trusteeships, etc.

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The form of application approved by the Board is intended to furnish an analysis of the character of business of the banks involved as far as it is possible to determine this from the books of the bank. The Federal reserve agent should supplement this, however, with any information he may be able to obtain and should base his recommendation upon the facts in each case. If he concludes that there is substantial competition between the banks or that interlocking directorates or common officers or employees of the two banks might result in any injury to the public, or in any substantial restraint of or detriment to the business of either bank, he should recommend that the application be refused. The Board, in reaching a decision, will carefully consider the recommendation of the Federal reserve agent and will base its conclusion upon the report and recommendation of the agent together with other information which its own investigation may disclose.

The Kern amendment authorizes the Federal Reserve Board at its discretion "* * * * to revoke such consent." In order that the Federal Reserve Board may revoke its consent at any time it becomes necessary, Federal reserve agents should keep it advised of any change either in local business conditions or in the resources or character of business conducted by the banks which may tend to make them substantial competitors.

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In view of the great amount of time necessary to an adequate consideration of each case it is desirable that directors, officers and employees file their applications as soon as possible. The Board will endeavor to act upon all applications received before August 15, 1916, on or before September 15, 1916.

6/23/16.

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RESOLUTION ADOPTED BY THE FEDERAL RESERVE BOARD.

Friday, June 23, 1916.

oOo

WHEREAS, It appears that the twelve Federal reserve banks have purchased in the open market bonds in excess of the amount which might have been allotted to such banks at the end of this quarterly period on the basis heretofore determined upon and announced by the Board.

NOW, THEREFORE, BE IT RESOLVED, That it is the sense of the Board that no necessity exists for enforcing the requirement provided for under Section 18 of the Federal Reserve Act at the end of this quarterly period ending June 30, 1916, and that it will not at this time require the Federal reserve banks to purchase any of those bonds which are offered for sale by member banks through the Treasurer of the United States under the provisions of Section 18.

BE IT FURTHER RESOLVED, That the Secretary be instructed to send a copy of this resolution to the various Federal reserve banks and to the member banks which have offered bonds for sale in order that they may be notified of the action of the Board in the premises.

6/23/16

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FEDERAL RESERVE BOARD

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

June 23, 1916.

Dear Sir:

For your information there is given below a copy of a resolution adopted by the Federal Reserve Board at its meeting today covering the separation of the gold order certificates making up the Gold Settlement Fund and Federal Reserve Agents' Fund.

RESOLVED, that the gold certificates comprising the Federal Reserve Agents' Fund and the Federal Reserve Banks' Fund in the Gold Settlement Fund shall hereafter be separated so that certain certificates shall be credited to each fund by number and transfers made upon the books of the Federal Reserve Board by both numbers of certificates and amounts in dollars, and

BE IT FURTHER RESOLVED, that any loss which may occur in the Gold Settlement Fund after June 23, 1916, shall be charged against the Federal Reserve Agents' Fund or the Federal Reserve Banks' Fund accordingly as ownership of the lost certificate shall by its number be indicated on the books of the Gold Settlement Fund.

Very truly yours,

Governor.

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M E M O R A N D U M .

WHY MEMBER BANK DRAFTS ON FEDERAL RESERVE BANKS SHOULD BE ACCEPTED BY ALL FEDERAL RESERVE BANKS FOR IMMEDIATE CREDIT AT PAR.

* * *

1. Through the establishment of the Federal Reserve System, (membership compulsory) National banks are obliged to carry their reserves in Federal Reserve Banks. Drafts against that account should possess all the circulating value their drafts had heretofore on any or all of their former reserve correspondents.

2. In the operation of the collection system an incentive to use for over-the-counter drawings, drafts on Federal Reserve Banks should be offered. These drafts, credited on member bank books when drawn will float for at least one day and offset through the clearing of float their equivalent in items charged.

3. In the operation of the collection system the balances between the Federal Reserve Banks are created by check transactions that are equivalent of gold through the Gold Settlement Fund. The exceptions to this are some payments received through local clearing houses, deposits of lawful money or rediscounts.

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4. Checking in anticipation or kiting can be controlled by reason of the supervisory relationship of Federal Reserve Banks to their member banks.

5. Through making a low open discount rate on dollar exchange, very much lower than open rates prevailing for sterling drafts on London, the Federal Reserve Banks are seeking to popularize acceptances of American banks in world centers. It is just as important to stimulate the use of drafts on Federal Reserve Banks in this country, even to the point of concession or some expense in the beginning.

6. Drafts on Federal Reserve Banks will be collected only through other Federal Reserve Banks for immediate credit. It amounts to the same proposition as draft on a branch presented through the parent bank or vice versa.

7. A settlement fund consisting of lawful money can be constituted in Washington if experience in immediate payments make it necessary or desirable. Details, such as charging the member banks reserve account with the draft on the day it reaches any Federal Reserve Bank, and bank transfers upon request only can be made part of the plan.

Postscript.

To the above might be added the following, as a supplemental reason :

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The public generally have been educated by experience to the fact that a draft on a New York bank is given immediate credit and is available for funds at any town in the United States or for that matter in North America. So true is this that a careful study of bank statistics shows that there are very few banks in the United States, National or State, that do not keep accounts in New York, the reason being that in no other way can they meet the wants of their customers in making payments at distant points. The question is whether this requirement will still be made, or whether a draft drawn by a member bank on its own Federal Reserve Bank can be made (by reason of the Gold Settlement Fund and telegraphic transfer) immediately available.

Many member banks maintain that reserves in Federal Reserve Banks will be worth little if this is not done. Furthermore, if it is not done, it is argued with some force that the Federal Reserve System, instead of decentralizing reserves, will tend to centralize them more than ever in New York City.

Is it not desirable that a draft on a Federal Reserve Bank should be popularized in every possible way, and that a member bank be justified in charging a moderate fee to its customer for such a draft ?

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So far as safeguards are concerned, there is no objection to surrounding them with all possible safeguards. For example, a member bank might be required to send, at the end of each day, by mail, to its Federal Reserve Bank a list of all drafts drawn against it, showing to what points they have been sent, if it is known. This would do away with "check kiting".

6/27/16

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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

June 29, 1916.

Dear Sir:

In response to my telegram of June 21, to each Federal Reserve Bank asking for views in respect to giving immediate credit at par for drafts drawn against Federal Reserve Banks, we have received replies from each bank, five of which are favorable, namely: Cleveland, Richmond, Minneapolis, Dallas and San Francisco; and seven are opposed, namely: Boston, New York, Philadelphia, Atlanta, Chicago, St. Louis and Kansas City. In view of this marked difference of opinion, the Board is undisposed to press the matter unduly at this time, but proposes to let the matter run along for further consideration.

The suggestion has been made by one of the Reserve Banks that this privilege should not be granted unless each Federal reserve bank maintains a substantial balance with every other Reserve Bank whereon its members may desire funds; the supposition being, however, that the balances would be maintained largely in New York. The Federal Reserve Board will, of course, have no objection to this, because the law permits the various Federal Reserve Banks to keep balances with each other for exchange purposes, but it may be pointed out at this time that the object of the Gold Settlement Fund was to keep a joint fund in Washington which could be classed as reserve

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and which would operate with greater smoothness and facility than for each bank to keep balances with eleven other banks. It has been stated that there is no necessity for haste in this matter, but it would appear that this is one of the problems which should have thoughtful consideration of the Executive officers and the Reserve Agents of each bank and be settled in the near future.

An important feature of the problem, is that after November, 1917, deposits in banks other than a Federal Reserve Bank are not reserves. These deposits, while drawing interest, must be continued if at all, as excess deposits.

The suggestion has been made by Mr. Harding, of the Board's Committee, that instead of insisting on any general ruling, each Federal Reserve Bank make its own arrangements so that drafts drawn against them would be given immediate credit at such Reserve Banks as they thought desirable. If, for example, the San Francisco Bank desired to have its drafts immediately available at par in Chicago and New York, it could make arrangements with the Chicago and New York Reserve Banks to effect this. This would be a partial if not complete solution of the problem which would perhaps answer the purpose for the present and till a more comprehensive plan is devised.

A fact not to be overlooked is that the public generally have been educated by experience to the fact that a draft on a New York Bank is given immediate credit and is available for funds

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at any town in the United States or for that matter in North America. So true is this that a careful study of bank statistics shows that there are very few banks in the United States, National or State, that do not keep accounts in New York, the reason being that in no other way can they meet the wants of their customers in making payments at distant points. The question is whether this requirement will still be made, or whether a draft drawn by a member bank on its own Federal Reserve Bank can be made (by reason of the Gold Settlement Fund and telegraphic transfer) immediately available.

Many member banks maintain that reserves in Federal Reserve Banks will be worth little if this is not done. Furthermore, if it is not done, it is argued with some force that the Federal Reserve System, instead of decentralizing reserves, will tend to centralize them more than ever in New York City.

It is not desirable that a draft on a Federal Reserve Bank should be popularized in every possible way, and that a member bank be justified in charging a moderate fee to its customer for such a draft?

So far as safeguards are concerned, there is no objection to surrounding these operations with all possible safeguards. For example, a member bank might be required to send, at the end of each day, by mail, to its Federal Reserve Bank a list of all drafts drawn against it, showing to what points they have been sent, or made payable, - which would be a safeguard against "check

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kiting". Furthermore, special safeguards might be required on transfers of funds or the making of drafts for large amounts say over ten thousand or twenty-five thousand dollars.

Yours truly,

Chairman, Committee on Clearing.

Statement enclosed.

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STATE	National Banks		State Banks and Trust Cos. not including Savings Banks and Private Banks.	
	Total Number	Number listing New York correspondent.	Total Number	Number listing New York correspondent
Oklahoma	351	251	556	134
Oregon	89	86	154	111
Pennsylvania	837	750	449	397
Rhode Island	18	17	28	28
South Carolina	71	71	319	283
South Dakota	112	74	494	77
Tennessee	117	116	396	245
Texas	536	518	890	621
Utah	23	23	87	74
Vermont	48	41	35	28
Virginia	137	125	282	179
Washington	80	78	282	227
West Virginia	117	113	190	171
Wisconsin	138	112	680	213
Wyoming	33	30	72	38
TOTAL	7,627	6,690	16,955	9,799

6/29/16

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714 b.

NUMBER OF BANKS LISTING CORRESPONDENT IN NEW YORK CITY

AS SHOWN BY BANKERS' DIRECTORY.

STATE	National Banks		State Banks and Trust Cos. not including Savings Banks and Private Banks.	
	Total Number	Number listing New York correspondent.	Total Number.	Number listing New York correspondent.
Alabama	92	92	258	254
Alaska	3	3	12	11
Arizona	13	13	66	62
Arkansas	67	51	395	121
California	261	252	354	304
Colorado	120	115	179	101
Connecticut	72	72	68	66
Delaware	24	11	24	12
District of Columbia	14	14	12	12
Florida	55	54	198	186
Georgia	112	111	654	639
Hawaiian Islands	5	5	17	8
Idaho	58	53	121	64
Illinois	472	351	807	320
Indiana	257	226	575	285
Iowa	348	248	456	201
Kansas	219	213	959	556
Kentucky	140	133	439	197
Louisiana	38	38	232	175
Maine	68	36	67	40
Maryland	97	79	108	60
Massachusette	169	122	85	75
Michigan	106	101	319	259
Minnesota	280	223	993	449
Mississippi	36	36	268	226
Missouri	133	96	1,293	295
Montana	69	61	217	109
Nebraska	197	169	815	506
Nevada	11	11	18	17
New Hampshire	56	30	13	2
New Jersey	204	195	137	123
New Mexico	37	34	44	31
New York	479	478	325	323
North Carolina	80	79	402	299
North Dakota	152	115	641	199
Ohio	377	366	480	417

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 5, 1916.

My dear Sir:

In the July issue of the Federal Reserve Bulletin there are printed all of the amendments which the Federal Reserve Board has sent forward to the Congress now in session.

Definite action has not been taken by Congress upon these recommendations. It is now so late in the session, and the work of Congress so congested, that the Board fears that unless those interested in the amendments make their wishes known to either Honorable Robert L. Owen, Chairman, Committee on Banking and Currency of the Senate, or Honorable Carter Glass, Chairman, Committee on Banking and Currency of the House, or both, there is danger that needed action may not be taken.

The Board believes the amendments are important and desirable and the situation is brought to your attention that you may state it to those whom you know to be interested.

While this letter is personal to you, the Board will be glad to have the assistance of your member banks or others who have an interest in the amendments and to this end to have them informed as to the progress made toward action.

It is hardly necessary to add that if, for any reason, any of the proposed amendments are not favored, the member banks should feel free to indicate their opinion as to them.

Very truly yours,

Governor.

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COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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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

T24

July 7, 1916.

Dear Sir:

Enclosed please find, for your information, copies of forms 94 and 94a which have been approved by the Federal Reserve Board, and copy of letter with which these forms are sent to applicants under the Kern amendment to the Clayton Act, for permission of the Federal Reserve Board to serve at the same time as director, officer or employee of a member bank and not more than two other banks, banking institutions, or trust companies which are not in substantial competition with the member bank.

Under separate cover copies of form 94b are being forwarded to you for use in reference to these applications.

It will be necessary for you to make a definite recommendation on each application and to forward it with all the other papers to the Federal Reserve Board for its consideration. If any of the institutions mentioned in the application are located in another Federal Reserve District you should prepare a copy of forms 94 and 94a and forward them to the Federal Reserve Agent of that district in order that he may make a recommendation and in turn forward them to this office.

Very truly yours,

Governor.

Enclosures.

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727

Washington, D. C., July 7, 1916.

WHY A DRAFT OF A MEMBER BANK AGAINST SURPLUS FUNDS TO ITS CREDIT IN A FEDERAL RESERVE BANK CAN PROPERLY AND SAFELY BE GIVEN IMMEDIATE CREDIT AT PAR BY ANY OTHER FEDERAL RESERVE BANK.

(1) Under the Federal Reserve Act, a member bank may carry a deposit in excess of its minimum reserve with its own Federal Reserve Bank, but is not allowed to carry a deposit with any other Federal Reserve Bank;

(2) A Federal Reserve Bank may carry a deposit "for exchange purposes" with every other Federal Reserve Bank;

(3) Under the conditions stated in (1) and (2) above, if a member bank draws a draft against surplus funds in its own Federal Reserve Bank, that draft could be cashed by the individual in whose favor it is drawn at any other Federal Reserve Bank if the Federal Reserve Bank against which it is drawn has a balance on deposit with the payee Federal Reserve Bank and has made the necessary arrangements;

(4) In order to make a draft on a Federal Reserve Bank immediately payable at any other Federal Reserve Bank, two important points would have to be safeguarded:

(a) The drawing bank would have to have sufficient surplus over minimum reserves with the Federal Reserve Bank against which it is drawn;

(b) The Federal Reserve Bank would have to have accounts "for exchange purposes", as specified in the Act, or some

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equivalent with every other Federal Reserve Bank.

(5) If every Federal Reserve Bank had an account with every other Federal Reserve Bank, it would mean that each of the twelve Banks would have to have eleven such accounts. In the aggregate this would mean one hundred thirty-two accounts for exchange purposes. Balances in the above accounts, however, would not count as reserves for the Bank to whose credit they were standing; and therefore, in order to simplify exchange operations and to permit Federal Reserve Banks to count exchange balances as reserves, the Federal Reserve Board more than a year ago agreed to keep in Washington a Central Gold Settlement Fund. Under the operations of this Fund, each of the twelve Banks was privileged to keep one account instead of eleven accounts. The operation of paying into, out from or transferring between Federal Reserve Banks in this Fund is familiar to all concerned;

(6) As above explained, the Gold Settlement Fund at Washington, through its twelve accounts, takes the place of one hundred thirty-two accounts which may be kept for exchange purposes and has the further advantage of counting as reserves for the depositing Bank, and of rendering a balance held in it available to meet obligations coming against a Federal Reserve Bank from any other Federal Reserve Bank.

The foregoing detailed statement makes sufficiently clear the existing facts. There still remain to be worked out some specific safeguards to protect Reserve Banks against overdrawing by member banks or "kiting" of checks. The safeguards proposed are as follows:

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(A) In order that a Federal Reserve Bank may be assured that its member bank is not drawing against funds non-existent, it shall be the duty of each member bank to list by mail each night the drafts drawn by it against its Federal Reserve Bank. When this notice is received by the Federal Reserve Bank, it might if it desired, make an immediate debit entry or memorandum entry against the drawer bank; but the amount thus entered should not be actually deducted in the analysis of accounts until the actual date of payment by a Federal Reserve Bank. It will be seen that this will effectively stop "kiting" and will require member banks to keep funds in excess of minimum reserves with the Federal Reserve Bank before they will be privileged to draw against them. It will, however, give the drawing bank advantage of the time which the holder of the draft may consume before presenting it for payment;

(B) In cases of drafts for large amounts - it is immaterial to the Federal Reserve Board whether the limit is placed at $5,000, $10,000, $25,000 or even higher - the drawing bank shall be required to notify the Federal Reserve Bank by wire, in addition to the mail advice above explained, stating at the same time at what point the draft is to be paid. The object of this rule is, obviously, simply to protect the Federal Reserve Bank and enable the Federal

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Reserve Bank to protect drawings for large amounts which may come against it.

IN CONCLUSION

Perhaps the two most important reasons for urging that drafts on Federal Reserve Banks be made available for immediate credit at par at any Federal Reserve Bank are -

(1) To make the draft on a Federal Reserve Bank the highest and most useful form of exchange and to thus give to member banks a facility not available to non-members and one which they can in their daily business use and appreciate; and

(2) To permit free flow of exchange operations so that the normal movement between different sections of the country may not be interrupted or diverted in such a way as to make necessary shipments of coin or currency between the Federal Reserve Banks; that is to say, Federal Reserve Bank "A" must receive items on Federal Reserve Bank "B" just as freely as "B" does on "A", otherwise offsets will not occur and currency shipments will be necessary. The recognition of this principle is essential to the complete success of the Board's clearing plan, for which the immense volume of items which will be handled, only a very free movement to and through Federal Reserve Banks will make certain the necessary offsetting of exchanges. The Federal Reserve Banks in the smaller centers can not well discontinue receiving bank

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drafts on New York and Chicago, as such drafts have been customarily received by all large banks and the refusal of a Federal Reserve Bank to so receive them would be strenuously opposed by member banks. The solution of the problem is for New York and Chicago to accept drafts on the other Federal Reserve Banks, with of course such precautions and safeguards as may be necessary. This will give them items to offset those drawn against them or their member banks. This is necessary to the complete success of the clearing plan and of the continued successful operation of the Gold Settlement Fund. At the same time this is made possible by the existence of the Gold Settlement Fund, since a claim against another Federal Reserve Bank is in effect a claim against the Gold Settlement Fund.

F. A. DELANO,

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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PAUL M. WARBURG
W. P. G. HARDING
ADOLPH C. MILLER

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD
728.

July 7, 1916.

My dear Mr.

I enclose a memorandum (Stencil #727, of July 7, 1916) which states my individual views on a matter which we have already been discussing in correspondence and which I should like to have you take into consideration in connection with your study of this question. This memorandum has not been submitted to the Board and therefore does not represent the Board's action. At the same time, I should like to have you consider it in connection with the whole subject.

It seems to Mr. Harding and to me that the Board can not long defer making a ruling on the matter. Already we are receiving complaints from member banks, saying that they have given up their New York accounts and find now that a draft on a Federal Reserve Bank is not given the same credit that a draft on a New York bank was. These complaints are certain to multiply as time goes on and I can not help feeling that with drafts on New York preferred over drafts on other Federal Reserve cities, the Federal Reserve Bank of New York will feel very serious drains through its Gold Settlement Fund. The way to meet this situation is by having offsetting items.

Yours very truly,

F. A. DELANO.

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

Dear Sir:

This will remind you that copy covering business conditions for the Federal Reserve Bulletin, to be issued on the first of next month, will be welcome in the office of the Federal Reserve Board not later than the of this month. Its prompt receipt will aid in getting the Bulletin out on time.

If you have not already forwarded a list of State member banks and non-member banks in your District, items on which can be handled at par, please include such a list with the other matter requested in this letter.

There have been sent you slips on which the Board requests that you fill in briefly answers to the questions covering conditions in general business, crops, bank clearings, and other indications of general trend. Please return one of these slips with each report of business conditions. They are desired for the purpose of making an accurate summary of conditions in the United States.

Very truly yours,

Assistant Secretary.

7/10/16.

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FEDERAL RESERVE BOARD

WASHINGTON

735

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 14, 1916.

Dear Sir:

You are hereby advised that the Federal Reserve Board has approved an increase in the discount rate on commercial paper running from 31 to 60 days of one-half of 1% for the Federal Reserve Bank of Chicago. The current rates at that bank are now as follows:

3½% for maturities: within 10 days

4% for maturities: from 11 to 30 days

4½% for maturities: from 31 to 90 days

5% for maturities: from 91 days to 6 months

The following increases in discount rates have been approved by the Federal Reserve Board for the Federal Reserve Bank of Kansas City, effective July 24th:

Commodity paper rate increased from 3% to 4%

Trade acceptance " " " 3½% to 4%

Ten day commercial paper rate " 4% to 4½%

Very truly yours,

Assistant Secretary.

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
739.
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

Dear Sir:

Where two or more persons desire to make application for the Board's consent, under the Kern amendment to the Clayton Act, to serve on the boards of directors of the same two banks, it will be sufficient if one Form 94a is filed by each bank for the first applicant and reference is made to this form by subsequent applicants desiring to serve on the same two boards, provided, however, if either bank is required to make a report of its condition to the Comptroller of the Currency or to the State authorities after Form 94a has been filed, a new Form 94a should be filed with the first application subsequent to such report. To complete the records of the Board and to facilitate its work it is desired that Form 94a shall ba filed by the two banks involved in each case where the question of substantial competition is to be passed upon. Thus if the same persons desire to serve on the boards of Bank A and Bank B and the first applicant has filed Form 94a for Bank A and also one for Bank B, subsequent applicants may refer to these forms until either Bank A or Bank B has been required to make a later report of its condition to the Comptroller of the Currency or to the State authorities.

If Form 94a has been filed by Bank A and Bank B, for applicants desiring to serve with these two banks it will not be sufficient for an applicant desiring to serve on the boards of Bank A and Bank C to refer to Form 94a filed by Bank A in connection with Bank B.

In attaching to Form 94a a copy of last report of condition, newspaper clippings of the last published report may be used by banks, provided the date is marked thereon and an officer of the bank certifies to the correctness of the copy.

Very truly yours,

W P G Harding

Governor.

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FEDERAL RESERVE BOARD

WASHINGTON

July 18, 1916.

Memorandum for the Board:

National banks are authorized by law to act as financial, and Federal reserve banks as fiscal, agents of the Government. In sustaining the constitutionality of Federal legislation on the subject of banking the court held that the Federal Government had the implied power to create banks as agencies or instrumentalities of the Government to be used in the conduct of its fiscal affairs.

The fiscal affairs of the Government may be briefly summarized as follows:

A. Collection of Revenues,

B. Disbursement of Appropriations,

C. Marketing of Bonds,

D. Refunding of Bonds.

The national banks aided materially in the marketing of bonds which are used to secure circulation. Machinery is furnished in the Federal Reserve Act for refunding these bonds. In the matter, however, of the collection of revenues and disbursement of appropriations the Government has utilized national banks to a limited extent only, and the present system which is a modification of the old independent treasury system is admittedly cumbersome.

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COLLECTION OF REVENUES

Collectors of customs and of internal revenue deposit collections made with national banks designated as depositories by the Secretary of the Treasury; with the assistant treasurers of the United States, and with Federal reserve banks. In making collections they are authorized to accept checks drawn on and certified by banks located in the same city as the depositary banks and such out of town checks as may be collected without expense to the Government. In practice the collectors of internal revenue frequently find it necessary to accept checks from almost any point in their respective collection districts. These collections are deposited the day received and the bank issues a certificate of deposit therefor in the name of the collector and credits the revenues to the Treasurer's general account, forwarding the original certificate of deposit to the Secretary of the Treasury through the office of the Treasurer of the United States, together with a daily transcript which shows receipts, the source thereof, and Government warrants and checks paid, the latter having been charged to the Treasurer's general account.

DISBURSEMENT OF APPROPRIATIONS

Under the provisions of Circular No. 5 all disbursing officers carry their accounts with the Treasurer of the United States, and draw checks against their respective balances, which have previously been placed to the official credit of such officers through

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an accountable warrant. These checks are honored by any depositary bank at par and as above stated are charged against the Treasurer's general account, forwarded to the Treasurer of the United States at the close of business each day, and when received by him are charged against the balance of the disbursing officer whose name appears therein as the drawer of the check.

Prior to the issuance of Circular No. 5, disbursing officers carried their accounts with the various Assistant Treasurers of the United States and with depositary banks.

OBJECTIONS TO PRESENT SYSTEM

Under this system of collections and disbursements the Public Monies Division of the Treasury Department is required to maintain a very large number of accounts on its books. These accounts must be carefully checked and the balances covered into the General Fund. The bank receiving the deposits from a collector issues its certificate which is sent through the Treasurer's office to the Secretary of the Treasury, Public Monies Division, and the amounts represented thereby are periodically covered into the general fund. If a check is received without certification and proves to be uncollectible or if a bank which has certified a check given to a collector fails before the check is paid, it is exceedingly difficult to make any proper adjustment, and the depositary bank must necessarily assume a certain risk in handling these collections.

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The method of requiring all disbursing officers to carry their accounts with the Treasurer of the United States is also open to criticism. I am informed that its operation is expensive and that it is in many respects unsatisfactory. The volume of checks constantly in transit is necessarily large, and these checks will normally remain outstanding even longer than the ordinary bank check. While it is necessary to maintain a large and expensive force to handle these checks when they reach the Treasurer's office, it appears to be impracticable for the present force to properly scrutinize and check the various items received before final payment is made and a certain unnecessary risk must therefore be assumed.

To illustrate, a disbursing officer in California draws a check on the Treasurer of the United States at Washington. This check is deposited in a bank in San Francisco; the San Francisco bank uses it to create exchange in Denver; Denver, in turn, uses it to create exchange in Minneapolis; Minneapolis may send it to Chicago, and Chicago to New York. When it finally reaches Washington it is necessarily covered with indorsements. The Treasurer's office before payment should first verify the signature of the disbursing officer, should see that the payee has indorsed it, that all subsequent indorsements are in order, and should check the object for which drawn which should be shown on the face of the check. I am advised, however, that with the present force it is not practicable to do this; that the signatures are not verified, the indorsements and object for which drawn are not checked, and that after checking the amount of each item against the account current

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sent in by the remitting bank, the checks are filed.

If it becomes necessary to stop payment on such checks under the present system it is very difficult to do so, and in view of the incomplete records of the Treasurer's office it is also difficult to trace any particular item after payment has been made.

SUGGESTED CHANGES

It is respectfully suggested that the accounts could be simplified and the collection and disbursements of revenues more effectively safeguarded if a plan substantially as follows should be adopted:

(1) The twelve Federal Reserve Banks have been designated as depositaries and fiscal agents of the United States Government. As such, they are authorized to carry funds to the credit of the Treasurer's general account. Under authority of Section 3620 Revised Statutes each Federal Reserve Bank might likewise be designated as a depositary for the accounts of all disbursing officers located in its Federal Reserve District.

(2) The designation of national banks as Government depositaries might be continued, but they should not be designated as depositaries for any disbursing officer.

(3) Collectors of customs and internal revenues might be permitted to deposit in member banks and such member banks might be authorized to issue certificates of deposit in the name of the Federal reserve bank of that district.

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Each member bank, as at present, could be required to furnish bonds to secure such deposits, to pay interest thereon, and to remit all in excess of such security to its Federal Reserve Bank. The deposits thus made in member banks would stand to the credit of the Treasurer of the United States with the Federal reserve bank and not to the credit of the Treasurer of the United States with the member bank. The certificates of deposit could then be forwarded through the Treasurer as at present and he could charge the amount represented thereby to the account of the Federal Reserve Bank. In this way he would be required to maintain only twelve accounts instead of several hundred as at present. All disbursements could then be made by check on the Federal reserve bank of the district in which the disbursing officer is located, and these checks could be handled as any ordinary bank check and could be safeguarded by the usual precautions taken in such cases. The twelve Federal Reserve Banks could then furnish accounts current at regular intervals to the Auditor for the Treasury Department. The Treasurer of the United States would charge accountable warrants to the various disbursing officers and credit them by notice of auditor's settlement.

I am advised that such a system would result in a saving of several thousand dollars in the expense of operation. The credit balances created in favor of the Federal Reserve Banks with the several national banks would materially reduce the transfer of funds incident to the collection and clearance of checks. A

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Federal Reserve Bank, for example, might check against a credit balance in a remote part of its district to pay a debit balance of another bank in that part of the district. The funds of the United States would be available in the parts of the country where they are most needed and a very much more scientific system could be worked out along these general lines than that now in force.

It may be possible that some slight amendment to the Federal Reserve Act would be necessary to authorize national banks to receive deposits for Federal Reserve Banks and to issue certificates in their name, but if the system is approved there should be little difficulty in procuring such an amendment, and I respectfully recommend that the question be taken up with the Secretary of the Treasury with the view of having the matter investigated and the details worked out for his consideration.

Respectfully,

M. C. ELLIOTT,

Counsel.

7/19/16.

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Chicago, Ill., July _____ 1916.

TO THE FEDERAL RESERVE AGENTS:

Your committee begs leave to report as follows:

It has visited the Federal Reserve Bank of Minneapolis, and has made an investigation of the system of public relations work in operation under the direction of Chairman Rich. It finds that the statements of this work made by Chairman Rich before the recent Third Conference are fully substantiated, and that the methods which he follows are producing very satisfactory results in District No. 9.

Your committee attaches hereto three memoranda prepared by Chairman Rich, one covering the scope and objects of public relations works, one covering the methods of public relations work in Federal Reserve Banks, and one covering suggestions for possible extensions of this kind of activity. It believes that so far as the details of the practical conduct of such activities are concerned, that they are well set forth in these memoranda.

As principles upon which these activities may be properly founded, your committee reports as follows:

1: This work should not be a casual or incidental part of the duties of the Reserve Agent. A man should be assigned to the work to give it such attention as is required and who will be charged with its responsibility. He may be a man who is already in the bank, who can be trained and developed, or, if necessary, a competent and experienced man can be hired from the outside. He should be a man who can demonstrate his judgment and discretion (preferably one who understands newspaper methods), and who can stand in a close and confidential relation

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to the Reserve Agent.

2: A system of cooperation should be established between the Reserve Banks that are best posted and are successfully prosecuting this kind of work, and the banks which are not so well posted and desire to engage in it. This would imply that the banks able to render assistance should hold themselves ready to contribute their advice and suggestions as requested by other Reserve Banks.

3: There should be a system for the interchange of material, information, ideas, methods of work, good suggestions, and the results, pro and con, of practical experience in these activities. The purpose should be to gather together all practical information and all the good ideas that develop in any Federal Reserve Bank and make them available to all the Reserve Banks.

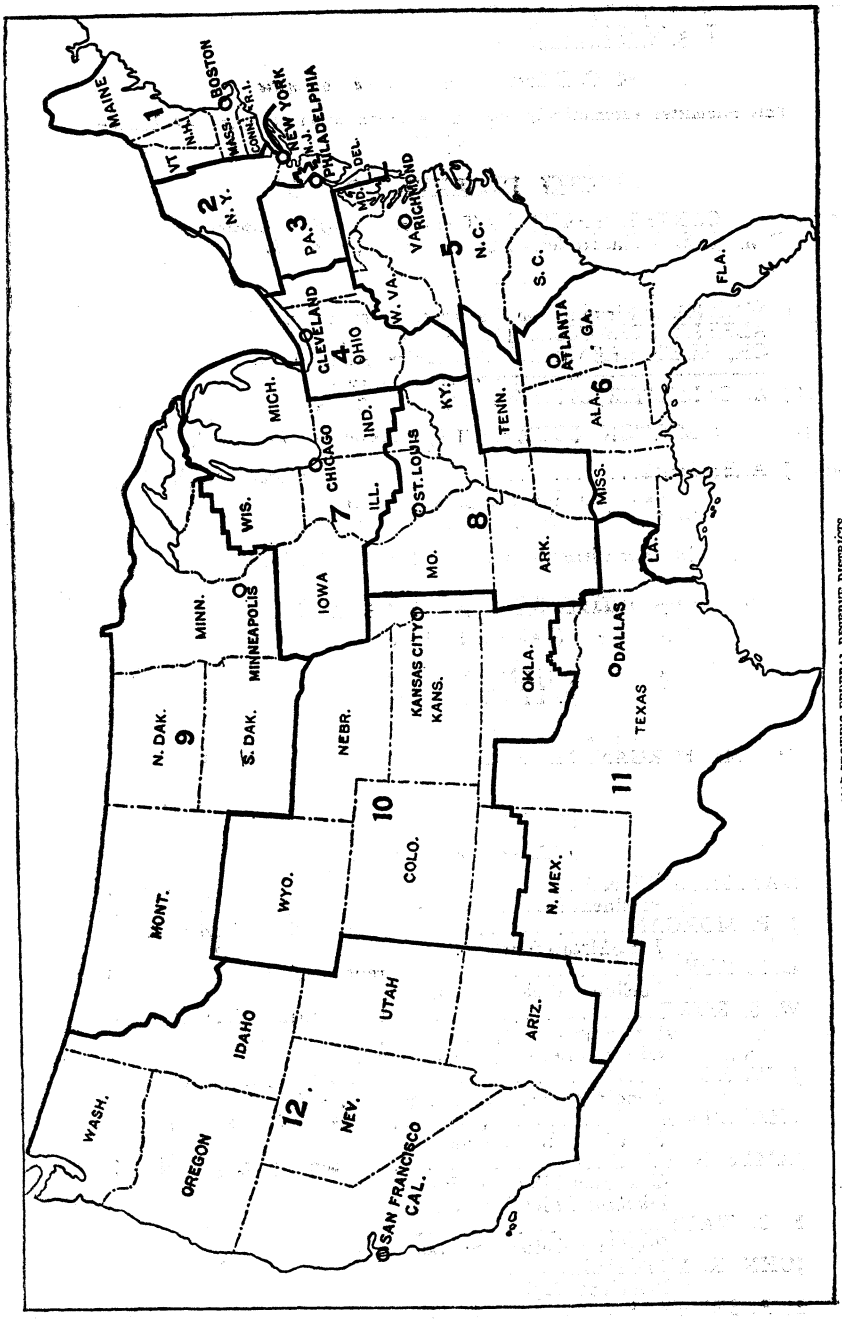
4: Such men as are detailed or employed on this work should be called together for a conference at Chicago, with Mr. Mosher of the Ninth Bank present.

5: Any moderate expenses that may arise out of the handling of the preliminary work of establishing activities along parallel lines should, with the consent of the Reserve Agent interested, be prorated upon the banks for whom the service is afforded.

As to the details, and the practical side of the establishment and conduct of this work, your committee does not believe it is necessary to report at this time, other than to call attention to the memoranda by Chairman Rich attached hereto, and to suggest that these will be settled according to the best judgment and experience of the Reserve Agents directly concerned, and the men whom they assign to this work, and

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THE FEDERAL RESERVE CITIES AND DISTRICTS AS MODIFIED BY THE FEDERAL RESERVE BOARD TO MAY 1, 1917.



MAP SHOWING FEDERAL RESERVE DISTRICTS.

Original decision determining cities and districts. ¶8.

Redistricting decision of May 4, 1915,—¶25. Changes of February 25 and February 29, 1916—¶26 and 27. Changes of October 13, 1916 (effective January 1, 1917) ¶28.

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THE RESERVE BANK ORGANIZATION COMMITTEE

W. G. McADOO, Secretary of the Treasury, *Chairman.*
D. F. HOUSTON, Secretary of Agriculture.
J. S. WILLIAMS, Comptroller of the Currency.

M. C. Elliott, *Counsel, and Secretary to the Committee.*

This committee automatically ceased its functions on the organization of the Federal Reserve Board, August 10, 1914.

THE FEDERAL RESERVE BOARD

CARTER GLASS, Secretary of the Treasury, *ex-officio, Chairman.*
J. S. WILLIAMS, Comptroller of the Currency, *ex-officio.*

W. P. G. HARDING, of Birmingham, *Governor.* Term expires Aug. 10, 1922.
ALBERT STRAUSS, of New York. Term expires Oct. 26, 1928.
CHARLES S. HAMLIN, of Boston. Term expires Aug. 10, 1926.
———————— Term expires Aug. 10, 1920.
A. C. MILLER, of San Francisco. Term expires Aug. 10, 1924.

MILTON COURTRIGHT ELLIOTT, *Counsel for the Board.*

J. A. Broderick.....*Secretary to the Board*
Louis C. Adelson, *Assistant Secretary.*
W. T. Chapman, *Assistant Secretary.*

For standing committees of the Board see p. 169, ¶231.

THE FEDERAL ADVISORY COUNCIL

(Law reference: Page 20, Law ¶92.)

JAMES B. FORGAN, *President.*
LEVI L. RUE, *Vice-Persident.*

Executive Committee.
Mr. FORGAN, Mr. RUE, Mr. MORGAN, Mr. WING, Mr. ROWE.

The Council.

To serve until December 31, 1918.

DANIEL G. WING.....representing District No. 1
President First National Bank, Boston.
J. P. MORGAN.....representing District No. 2
J. P. Morgan & Co., New York.
L. L. RUE.....representing District No. 3
President Philadelphia National Bank, Philadelphia.
W. S. ROWE.....representing District No. 4
President First National Bank, Cincinnati.
Director Federal Reserve Bank of Cleveland.
J. W. NORWOOD.....representing District No. 5
President Norwood National Bank, Greenville, S. C.
CHARLES A. LYERLY.....representing District No. 6
President First National Bank, Chattanooga.
JAMES B. FORGAN.....representing District No. 7
Chairman First National Bank, Chicago.
Director Federal Reserve Bank of Chicago.
F. O. WATTS.....representing District No. 8
President Third National Bank, St. Louis.
JOHN R. MITCHELL.....representing District No. 9
President Capital National Bank, St. Paul.
E. F. SWINNEY.....representing District No. 10
President First National Bank, Kansas City.
E. P. WILMOT.....representing District No. 11
President Austin National Bank, Austin, Texas.
HERBERT FLEISHHACKER.....representing District No. 12
President Anglo & London-Paris National Bank, San Francisco.

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that these matters will adjust themselves in the orderly development of this subject.

In conclusion, your committee begs leave to report that the system of work employed by Chairman Rich is productive of substantial results for the Ninth Bank, and is of such a character that it can be adapted as conditions may necessitate, and applied in any Reserve District. Conducted with judgment, keeping in mind that such publicity might be misconstrued and harmful to the system, and with careful attention to the purposes which it can be made to serve, your committee believes that this is a desirable work, and that all the Federal Reserve Banks might well engage in it, but would suggest that great care should be given in establishing it to provide for such conduct and supervision of the work as will guarantee that it is properly founded and that it begins with the best opportunities of success.

It would probably be advisable, in view of this suggestion, and where this work is new, that it be introduced upon a moderate scale and expanded as experience may warrant.

Respectfully submitted:

C. H. BOSWORTH, Chairman,
WILLIAM McC. MARTIN,
CHARLES M. SAWYER.

7/20/16.

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PUBLIC RELATIONS WORK IN THE FEDERAL RESERVE BANKS.

By John H. Rich.

1 - SCOPE AND OBJECTS:

GENERAL. The strength of the Federal reserve system will be in a measure proportionate to the confidence of the general public in the respective Federal reserve banks. Each reserve bank performs two kinds of functions. The first, of a purely banking sort, relates almost exclusively to the member banks. When these have been discharged, practically all of the remaining activities of the bank are of a character that directly affect the welfare of every citizen. Because of the very broad public service the reserve banks are designed to render, it is desirable that they have at all times the best and most substantial degree of public support and confidence. Such support will be limited unless it is possible for the public to clearly understand and appreciate the service that the reserve banks are rendering.

Public relations work aims to create conditions under which a Federal reserve bank can operate with the best degree of efficiency. It seeks the cooperation and support of the public and the friendly interest of the member banks. It aims to create a favorable public opinion and to awaken an appreciative interest among members, and having accomplished those purposes, to direct this opinion and interest in such a way as to best serve the purposes of the reserve bank.

In seeking to intelligently direct public opinion, it exerts at the same time an educational influence, that the support thus created may not only be substantial, but intelligent as well.

OBJECTIVES: Public relations work should not be undertaken without definite objectives. These objectives may be:

(a) The building up of state bank membership.
(b) The education of members to the proper use of discounting facilities.
(c) The education of the public as to the public service, as distinguished from the banking service, rendered by reserve banks.
(d) Preparing the way for the introduction and use of new facilities, such as trade acceptances, etc.
(e) Facilitating the introduction of enlarged facilities as represented by the par collection of checks.
(f) The education of the public as to the significance of the functions performed by reserve banks, and the intelligent employment of such facilities as it affords for public use.
(g) Correcting and directing the trend of opinion among member banks.
(h) To exert the requisite degree of control upon both public and banking opinion in matters affecting the development of the reserve banks in their own field.

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These purposes will alter and change as the requirements of each reserve bank may determine. Considered as suggestions, they serve to indicate that public relations work along the right lines can be made very servicable.

This line of effort may be considered in both an offensive and defensive light. It has already proven an effective weapon against ill-considered and unjustifiable criticism; while on the other hand, it has had great usefulness as an educational instrumentality, both with the public and with member banks.

"PUBLICITY" There is a sharp distinction between publicity and public relations work. Publicity is ordinarily considered to consist of a little more than the preparation of material which newspapers are persuaded to print. Public relations work, as herein contemplated, is of a broader and more serious character. So far as the Federal Reserve Act is concerned, and the regulations of the Federal Reserve Board, it is clear that a Federal reserve agent might capably and efficiently perform all the duties that are specifically assigned to him, and still occupy in a Federal reserve bank a position involving no duties that could not be discharged by an experienced auditor of requisit character and integrity. The Federal Reserve Board was empowered to exercise very close supervision over the operations of each reserve bank, and was established as a governing and controlling authority. Within broad lines, it has delegated this leadership and authority, in each reserve bank, to its representative, the Federal reserve agent. The responsibility for leadership, in all the broader activities of the bank, therefore falls upon the Federal reserve agent.

THE FEDERAL RESERVE AGENT: Public relations work is practically the foundation upon which the Federal reserve agent is to perform this service. He can not work effectively without a receptive attitude on the part of member banks, nor can he efficiently cover the broad field assigned to him without the friendly interest of the public. While he will have the active and valuable cooperation of the Governor, and of the other members of the banking staff, the responsibility of leadership naturally falls on him, in the task of building up State bank membership and working toward the creation of a single banking system, in the slow process of creating relations with member banks under which the reserve banks can build up a volume of business and acquire their maximum usefulness and efficiency, in the preparation of the way for the introduction of new ideas and new methods, and in the large field that is represented by the contact of the reserve agent, as the representative of the supervising and governing authority in Washington, with the public. Public relations work is in a large measure the work of creating conditions under which these responsibilities can be discharged with the best effectiveness.

Each Federal reserve bank has been handicapped since organization by certain obstacles, among which is a lack of clear and precise

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undertaking of the law among the member banks themselves. The provisions of the Act are not understood. Its purposes are not clear, especially to the country bankers, and there is a deficient knowledge on their part of the working of the reserve banks. Because of this lack of knowledge they are fair prey to every criticism of the reserve system, whether well founded or not, and it is noticeable that even at this time many of them believe that the reserve banks are purely emergency institutions, that the country banks ordinarily have no paper of the right kind for rediscount, that the system of rediscount is involved and difficult, that contact with the reserve banks involves such red tape, that the reserve banks are too expensive in operation, that the check clearing plan is improperly founded, that it is an injustice to deprive them of exchange charges and of interest upon balances with correspondents, that the drift and tendency of the reserve system is to cut interest rates without compensating advantages, and that they have been handicapped, so far as the National banks are concerned by being compelled to enter a system in which membership involves difficulties and loss of profit, and does not provide new opportunities for satisfactory earnings. It is apparent that there is a large amount of slow, hard work that must be done before the first point - that of creating a satisfactory working understanding with members - can be realized.

A reserve bank that is not equipped to meet these objections or to face annoying situations as they may arise, from time to time, must necessarily exhibit a certain degree of helplessness. It is fair at least, to conclude that the progress of the reserve banks, the development of the volume of business with members, and to some extent, the growth of their earnings, will be proportionate to the ease and facility with which these misunderstandings can be cleared away and causes of friction eliminated.

While much misunderstanding has already been eliminated, it is very likely true that each new regulation of the Board and each new attenpt to broaden the activities of the reserve banks will create its own problems, the solution of which will be simplified where the creation of such problems is foreseen and adequate steps taken in advance.

The vital defect of most of the campaigns of public relations work undertaken in the United States in the last 15 years is that those interested have waited until the last moment before acting. They have then asked expert men to do the impossible thing of changing public sentiment, after it has already shown a distinct set in the wrong direction. Public relations work in time would have been much less expensive and vastly more productive, in numerous familiar instances.

ADVANTAGES: There are certain advantages on the side of the Federal reserve banks in any work of this character. The popular mind regards them, at least to a very large extent, as Government banks. The public usually supports the Government. The reserve banks have had a favorable introduction to the people. It is comparatively easy to augment this friendly interest. It is very noticable that in the work so

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far undertaken, help is being received from the most unexpected sources. In behalf of the Federal reserve banks, it has been possible to avail ourselves of the active assistance of very many men who, because of their own responsibilities and business activities, would ordinarily be quite indifferent. The willingness to extend such support is particularly noticeable on the part of the press - it seems to be almost a fixed rule that these banks are entitled to and must receive editorial support.

The peculiar organization of the Federal reserve system presents both advantages and disadvantages. It is clear that a centralized system of public relations work would always be at some disadvantage through the inability of an officer in Washington to intimately know the conditions in each district, and properly take advantage of them. Without the most careful supervision, there would be the inevitable tendency that manifests itself in other departments of Government activity, to allow such work to fall into routine lines with resultant loss of efficiency.

PLANS OF WORK: The Federal reserve banks are so located, geographically, that the problem of creating harmonious and uniform lines of work in the twelve different institutions presents difficulties.

To indicate the details of an effective and inexpensive system of publicity, in a suggestive memorandum, would be purposeless. The best judgment would, however, agree upon the following general features:

1. While the work in each of the reserve banks should be conducted along harmonious lines, the adoption of the same plan, with the same details, for each institution, is not practical and would not produce results.

2. Each reserve bank should therefore conduct its work as an independent unit under some form of central supervision or cooperation that will provide for an interchange of ideas and methods, and insure the direction of these twelve forces along lines that will produce harmonious results.

3. While still preserving the independence of each reserve bank in the conduct of its own work, it would be possible, without the expenditure of either a great deal of money or effort, to acquire a knowledge of conditions in each district, to advise in the selection of men in each reserve bank who could be educated to do a large amount of good work, and to establish some plan for the exchange of the best ideas and methods. If centralized cooperation had no other object than to create a clearing house for the gathering and distribution of good ideas, it would be of great value to each reserve bank.

A considerable amount of such material would, in the nature of things, be just as available in all the reserve districts as in any one. It is essential that the cost of such work be kept within the narrowest possible limits. Due to the natural advantages that the Federal

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reserve banks have, the expense of the work so far conducted by the Ninth Reserve Bank has been insignificant. This serves to illustrate the practicability of creating methods for each of the other reserve banks that will involve little, if any, expense.

It will probably be difficult to bring about harmony of action between the different reserve banks and secure the adoption of similar methods of work, unless the subject is taken over by some central committee in behalf of the different reserve agents. Such a committee could inform the different banks of the plans and methods which it believes to be practical, and could suggest ways in which the twelve banks might work along parallel lines. Under the supervision of such a committee, it would be comparatively easy to gather together and sort useful material, so that each bank might be put into possession of the good ideas that come to the attention of any one.

In conclusion, it seems to be clear that the most effective method of work will be that of making each reserve agent responsible for the the public relations work in his own district, but with such expert help as can be afforded him, and with such cooperation as will insure uniformity and the best results. The volume of work involved in each case will probably not be great, and would not ordinarily require the employment of additional help. It would probably prove true that there are men in the reserve banks who, with proper coaching and some training, can be made very effective in this line of work.

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LINES OF PUBLIC RELATIONS WORK OPEN TO FEDERAL RESERVE AGENTS.

By John H. Rich.

GENERAL: Advantage should be taken of the local characteristics of the district. Where there are commercial centers, there are commercial organizations. Where there are transportation centers, there are traffic organizations. Where there is a center for distributing business, there are strong credit organizations. Even in small towns, there are numerous kinds of growers' and producers' associations, each interested in a special kind of activity. Banks are usually grouped by districts, and hold periodic association meetings. In large centers where banks are numerous there are usually bankers' clubs. Spotting a map of a reserve district, with dots indicating the location of class, public and special organizations of business men and farmers, will indicate that the points at which there are organized groups of men who are active in agricultural production or in business and banking, are numerous and well distributed.

These points indicate opportunities of reaching the public. With slight effort, the reserve agent can arrange to address such organizations on questions that broaden the public knowledge of the Federal Reserve Act and the operations of the Federal Reserve Bank. One successful effort is usually followed by invitations opening the way to another. As this kind of work grows, information spreads rapidly and the Federal Reserve Bank is brought into touch with the leaders in numerous communities, and with those who form public opinion. This line of work has been carefully followed since the organization of the Ninth Bank with the result that more than 125 such addresses have already been made, largely by the Reserve Agent, and his assistant, reaching audiences representing banking and all classes of business. In the Ninth Bank we have even gone so far as to address one or two of the representative Labor Unions, using for a subject, the influence of the Reserve System in creating stable conditions of employment and in protecting labor from losses, such as usually follow periods of stress. The difficulty has not been to find representative bodies through which to work, but to take care of the invitations that come.

It should be borne in mind that the audience reached by the speaker is comparatively small. Because of this, it has been the practice of the Ninth Bank to prepare manuscript addresses. Copies of these manuscripts have been prepared and given to the newspaper press for release upon the day they were to be delivered. While the Reserve Agent may have spoken to 100 men, the address, when printed, has been carried very frequently to the remote corners of the district, and has reached many thousands of people. In fact, one of the reasons for making public addresses is the incidental opportunity to reach an immense number of business men through the public press, with a condensation of the practical information presented verbally. It has been found valuable to

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occasionally print and reproduce addresses in pamphlet form, for the purpose of summarizing the useful activities of the reserve banks from time to time.

It is our practice to maintain a special mailing list covering business men and others in the Ninth District, who are influential and who have a special interest in the Reserve Bank. Where friends and acquaintances are made through public addresses, or through other forms of work, their names are carefully recorded and they are supplied from time to time with material of this character to read at their leisure, and with which to refresh their minds on the progress the institution is making.

An investigation of the district will reveal the location and limits within which each principal newspaper has influence. On spotting up the map, it becomes easy to ascertain what selection of newspapers cover the district as a whole. Where there are gaps and vacant areas, it is possible to fill them in by selecting the best of the local publications. By this process, a closely restricted list of newspapers can be built up, which to the certain knowledge of the Reserve Agent will reach all parts of his district and the business men and farmers therein. Personal touch with the editors of these selected newspapers - always without solicitation of services - soon builds up friendships that open a convenient way to the use of the news and editorial columns of such papers. This process soon affords a dependable newspaper list, which will not only use what is given it in the way of statements for publication, but will solicit information and voluntarily open the way to reach their readers. The value of the process is that it avoids the necessity of broadcast requests for the publication of Reserve Bank news. It frees the bank from any criticism that it is "seeking publicity." This process gave the Ninth Bank the equivalent of 61 newspaper pages of good material in nine months, and was then utilized only in an incidental way and without any special effort.

Reserve banks are public in a sense. The average man is interested in them. It should, therefore, be the policy to satisfy his interest by giving him all the information of their current operations, etc., that can be released without embarrassment to the bank or its interests. Such news, if properly brought to editorial attention, is more valuable to the newspapers than the average grind of commercial bank news, because of the interest of the public above referred to. Reserve banks have contact with a broad field and are in a position to collect much more valuable information than the ordinary commercial bank. Friendly relations with the newspaper press are usually founded on a give and take process. The press expects news. The Reserve Agent who keeps this in mind, and is judicious in his selection of the newspaper representatives with whom he will have friendly relations, will have no difficulty in having the work of his bank brought to public attention. This applies more particularly to the larger newspapers in centers where reserve banks are located.

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It therefore appears that the Reserve Agent should have an accurate knowledge of the organizations of his district, and should take membership in a few of the best, distributing such memberships in such a way as to have personal touch with banking, credit, general business, traffic, producers and farmers associations. These membership relations will give him opportunities for promoting sentiment and stirring up beneficial discussion which will come without effort. He should be represented in the best local commercial organizations and should take an interest in its work and serve on its committees as a matter of policy.

He should spot up a newspaper map of his district and get on the proper personal footing with the important editors. He should have a good knowledge of their work, the policies of their papers, and the subjects of special interest to them. He is thus equipped to develop publicity opportunities along the most effective lines. He should invite such editors into his bank, and seek to have them learn from personal observation how a Reserve Bank works and what it does. The education on both sides is valuable, and soon produces opportunities for cooperation that bring results.

The daily progress of the reserve bank should be watched with the question in mind, "What is there here that the public has a right to know and would be interested in?" The dissemination of such information as can properly be released, produces a constant stream of information, going out through the medium of reporters for the local press who call daily, or should do so. Where matters occur that justify broader newspaper attention, statements should be made, and mailed, marked for release locally out in the district, on the same date and at the same hour. The outside newspaper is jealous of the better facilities of the local newspaper, and appreciates equal courtesy and equal treatment.

Cooperation with the newspaper press can be indefinitely extended. Press associations form an extremely valuable channel through which the public can be given information about the current activities of the Reserve Bank. In the Ninth Reserve District, the bank and the important press associations are working in cooperation, and the reserve bank articles are sent for use every Monday morning to all of the daily papers served by the association, and are condensed in shorter form for all the weekly papers. The newspapers thus served amount to 800.

Through cooperation with a leading daily newspaper, a reserve bank article, which is prepared so that it contains something fresh and up-to-date for each Monday morning issue, is duplicated by the newspaper in advance and forwarded, at its expense, to some 63 daily newspapers within the district. The article appears in Minneapolis, and in these outside newspapers, in the morning issues of the same date. The system has been found to give some prestige to the strong Minneapolis newspaper that affords this service, and has been very valuable in spreading information about the Ninth Bank.

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These Monday morning articles take up subjects of current interest, such as the development of the check clearing plan, the acceptance question, and other developments that are of public interest and importance.

The directorates of principal banks should be listed. The names usually form a pretty good list of the best men in each community. These lists, carefully revised, can be kept within moderate limits and still show the names of the men whose opinions count. These men should be supplied at intervals with comments of value on the Reserve System, or the bank of the district. When this work is carefully done for a six months' period, it usually begins to appear that there has been valuable discussion as a result. The cost is negligible.

Agricultural organizations should be listed in the same way, with careful selections of the men who are influential in shaping their policies. Such lists are invaluable at times and are of frequent use for the distribution of pertinent material.

Officers of trade and commercial organizations, with their directors, form an additional list of value.

Observation and discussion would indicate that the general subject of public relations work could be very greatly assisted if Reserve Agents would take the time and trouble to get out over their districts occasionally, and talk to their more important members, and the more influential business men at local points, in their own offices. Where such visits occur, it is noticeable that the local people are very appreciative. Usually the opportunity of saying an effective word, or clearing up misapprehensions presents itself. Even in the larger districts, the important centers, at least, could be reached in this personal way, once a year or so. Where there are districts in which not more than a third of the member bankers have ever been inside the Reserve Bank, this work ought to be especially productive.

Summarizing the subject: The Reserve Agent can not afford to press public relations and publicity work to a point where his effort is apparent. His position and responsibilities are important and dignified. He should rather, by quiet and judicious work, seek to have opportunities for accomplishing these results, present themselves without his solicitation. This can be done with little effort, through the systematic building up of the right personal relations. He should keep in mind at the same time, the interest of the public in the Reserve Banks, and seek to have his list of callers include not only bankers who want to talk about rediscounts, but business and professional men, manufacturers and others, who are influential locally, with whom he can discuss what the Reserve Bank is doing to facilitate business and support the current activities of the district better than before.

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SUGGESTED EXTENSIONS OF PUBLIC RELATIONS WORK.

By Mr. John H. Rich.

Once properly established, public relations work in a Federal Reserve Bank may be indefinitely extended. The growth of these activities, the manner in which they may be adapted to the opportunities presenting themselves from time to time, or to the changing necessities of the Federal Reserve Agent's work, is limited only by the fertility of ideas and the proficiency of the men to whom the work is assigned.

As an indication of the manner in which the activities previously outlined may be extended, the following suggestions are offered:

The Reserve Agent, or his representative, should get out over the district occasionally to renew acquaintances with newspaper owners and editors for the purpose of building up and renewing the friendly relations from which opportunities for the use of newspaper space are a natural outgrowth. This contact is very valuable, and is usually followed by the development of an interest on the part of the editor that prompts him to offer his ccoperation.

The stronger state banks should be visited. Where there is a lack of interest in membership, the local newspaper medium should be used to carry Reserve Bank articles with reference to membership of state banks, for the purpose of stirring up interest on the part of bank depositors and bank directors, which is oftentimes effective when the bank officers themselves are indifferent.

The crop and business reports rendered each month can be perfected and made more interesting, and it is suggested that it would be desirable to issue them in attractive, but inexpensive, printed form,

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and use the opportunity to insert on the back page a few paragraphs each month explaining the development of the Reserve System, and the progress of the particular Federal Reserve Bank. If this is done, the report should then go to a substantial list of the best and most influential men in the district for the purpose of reaching non-banking, as well as banking sentiment. It is desirable to keep closely in touch with the more important commercial organizations, such as trade bodies and Chambers of Commerce, and to have knowledge of the time of their annual meetings and the manner in which their programs are made up. This contact will afford frequent apportunities for the Reserve Agents to reach influential men with addresses, or should it prove practical, to invite to his district the agent of some other bank to present the Federal Reserve subject from a somewhat different angle.

Addresses of this character should be put in printed form for the purpose of utilizing them to present periodic summaries of the results of the operation of the Reserve Bank, and the service performed for members and the public. With this in mind, the Reserve Agent might easily include, at intervals of three or four months, a review of the progress of his bank, issuing the address, when ready for mailing, to a list of the more substantial business men, as well as the more important member banks. In this manner, the Reserve Agent is able, from time to time, to reach business men with fresh information about the bank, and to attract and hold their interest.

Where the district is largely agricultural, as is the case with the Ninth District, an occasional address devoted largely to

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practical discussions of the Reserve Bank in relation to agriculture, could be used to great advantage by putting it in printed form, and forwarding it to the influential farmers in each locality. Lists showing who these men are can be compiled without great effort, and should be included in the file of mailing lists in each Reserve Bank.

It is clear that concerted work to interest the public in trade acceptances would be very valuable. The same practical application of public relations work may be made in efforts to interest the public in the purchase of conversion bonds.

While the Federal Reserve Agents will naturally feel a hesitation in speaking outside their districts, it will be very possible for each Reserve Agent to call in the Chairman from some other district to occasionally address business organizations where the occasion is of enough importance to justify it. It will probably become increasingly desirable, as these banks are older, to present the subject from new angles and to give it an element of freshness. There seems to be no reason why the Reserve Agents should not respond to invitations transmitted through their colleagues.

Once established, public relations work should be prosecuted with the idea of continually refining the methods employed, and of making increasingly exact classifications of lines of work open in a particular district. This would involve, so far as the newspaper and periodical press is concerned, an effort to satisfy editorial demands with articles having a practical application to the class of people reached by the publication. As this work is undertaken, a

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very broad field opens up, and the ability of the Reserve Agent to reach individual business men is limited only by his ability to prepare special articles adapted to the uses of the particular publications which such business men read. In a special line of work such as this, it is naturally very difficult to duplicate the article and use the same text in a number of different publications.

As a concluding suggestion, it should be the established rule in the Federal Reserve Agent's department that every communication to the press that is of any consequence be handed to the newspapers in written form. No other method presents itself that will guarantee that the statements made with reference to a subject that is necessarily somewhat technical will go into the columns of the newspaper without being garbled and without showing embarrassing misstatements.

Where public addresses are delivered, it is highly desirable that the Reserve Agent have his address in manuscript form, and that he prepare duplicate copies for newspaper use. By this method he safeguards himself from the inaccuracies that are sure to creep in where reporters have no copy to follow and translate the address into their own language.

It should be the inflexible rule in the department of each Reserve Agent, who undertakes this work, that no statements or communications of any kind are to be released for publication until he has personally examined them. The Federal Reserve Agent is, after all, the one who must bear the brunt of any misstatements, and irrespective of how much confidence he may feel in those associated with him in his work, he should insist that this rule be followed. Copies of all newspaper

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statements, all articles prepared for publication, and all addresses delivered, should be retained in the files for future reference and use. By following this system the Reserve Agent has at all times a complete record of everything he has said and is in a position to conclusively meet any criticisms or any questions involving his public statements.

In giving out addresses for publication in the newspapers, it should be remembered that the average newspaper has no space for a document as long as a forty-five minute address. The Reserve Agent should, therefore, condense his address to a space of not more than 2,000 or 3,000 words, including therein his salient points, and this should be the copy given to the newspaper for publication. This process assists the editorial department, because it relieves them of editing an immense amount of material that in the nature of things can not be available for publication.

In summarizing this question, it is well to add the comment that work with newspapers and publications is an important feature of public relations work. It naturally follows that if articles are to be written for the press they ought to be the kind of articles that the press is anxious to have. This involves that they must be "good newspaper stories."

There is always the question whether a man who has not had the benefit of newspaper training can write a properly constructed newspaper article. Where Federal Reserve Agents have available bright young men with some ability to write, it would probably be possible,

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by coaching and training them, to very considerably increase their ability to write good newspaper articles. The best efficiency would probably not be attained, except where it is possible to utilize untrained men of exceptional ability, without assigning this work to men of seasoned newspaper experience and judgment. Newspaper ability alone is insufficient, because of the large amount of technical knowledge such a man must have. The problem of finding men having the right combination of experience, knowledge of the Reserve Act, and the operations of the bank, and the proper judgment and ability, will very likely present some difficulties. But such men will not be required except in banks where the Reserve Agent has determined to adopt this form of work on a thorough and comprehensive scale. Where a more limited form of public relations work is undertaken, the problem of finding men can probably be solved by putting them into touch with the men already in the work, who can impart to them something of their own experience and training, watch their work and advise with them, and give them practical assistance.

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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

July 20, 1916.

S i r :

Your attention is directed to an order issued by the Postmaster General bearing this date, directing postmasters to receive from Federal Reserve Banks checks on non-member banks for collection and remittance by registered mail to the Federal Reserve Banks.

It is desirable that Federal Reserve Banks should, as far as possible, collect checks through banks, but in cases where non-member banks in towns having no member banks, are unwilling to remit to Federal Reserve Banks at par, you will be permitted to avail yourselves of the facilities afforded by the Postmaster General's order. We hope, however, that it will not be necessary, as a rule, to make collections through post offices, and in cases where you feel obliged to make collections in this way, you should first arrange for fidelity bonds on the postmasters making collections, premiums on such bonds to be paid by your bank as well as postage and registration fees. This matter was taken up several months ago with some of the leading bonding companies, and the Board is informed that these companies are prepared to furnish proper bonds on reasonable terms. It is the belief of the Board that after the banking community has knowledge of the Postmaster General's order, many non-member banks that have hitherto been unwilling to remit at par for their checks, will agree to do so; but it is suggested that it would be well for your bank to enter into negotiations at once with the bonding companies, as the postmasters' bonds now held by the Postoffice Department do not cover such transactions as the collection of checks.

Very truly yours,

Governor.

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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

July 21, 1916.

S i r :

An order has been issued by the Postmaster General bearing this date, directing postmasters to receive from Federal Reserve Banks checks on non-member banks for collection and remittance by registered mail or money order to the Federal Reserve Banks.

It is of course desirable that Federal Reserve Banks should, as far as possible, collect checks through banks, but in cases where non-member banks in towns having no member banks, are unwilling to remit to Federal Reserve Banks at par, you will be permitted to avail yourselves of the facilities afforded by the Postmaster General's order. We hope, however, that it will not be necessary, as a rule, to make collections through post offices, and in cases where you feel obliged to make collections in this way, you should first arrange for a blanket insurance policy to cover all post offices making collections in this way, premiums on such insurance policies to be paid by your bank as well as postage and registration fees, or cost of money orders.

This matter was taken up several months ago with some of the leading bonding companies, and the Board is informed that these companies are prepared to furnish blanket insurance policies on reasonable terms. It is the belief of the Board that after the banking community has knowledge of the Postmaster General's order, many non-member banks that have hitherto been unwilling to remit at par for their checks, will agree to do so; but it is suggested that it would be well for your bank to enter into negotiations at once with leading bonding companies, as the postmasters' bonds now held by the Postoffice Department do not cover such transactions as the collection of checks.

Very truly yours,

Governor.

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

Suggested Circular.

The attention of the Board has been called to the fact that some of the State banks and trust companies have construed Circular No. 14, and Regulation M, Series of 1915, as indicating an intention on the part of the Federal Reserve Board to impose, by regulation, restrictions on the activities of State banks and trust companies which become members of the Federal Reserve System which are not imposed by the Federal Reserve Act or by the laws of the State under which such banks are organized. In order that any misapprehension on this score may be removed it is deemed advisable to further elaborate the purposes of the circular and regulation referred to.

The regulations of the Board will be designed to carry out the purposes of the Federal Reserve Act. State banks and trust companies becoming members of the Federal Reserve System are entitled to the privileges of member banks and are subject to those restrictions and limitations contained in the Federal Reserve Act which refer specifically to State banks and trust companies or which refer generally to member banks. Such State banks and trust companies are likewise subject to the laws of the State in which they are created and organized. In general, they must conform to the specific provisions of Section 9 of the Federal Reserve Act, to the reserve requirements contained in Section 19, and to those provisions of the Act which specifically refer to member banks.

It is not the purpose of the Federal Reserve Board to attempt to

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impose by regulation any restrictions on the activities of State banks and trust companies which become members of the Federal Reserve System that are not imposed by the Federal Reserve Act or by the laws of the State in which such banks are created and organized.

The scope of the corporate powers of State banks and trust companies is determined by the laws of the State under which they are created, and as members of the Federal Reserve System those powers are limited or restricted only so far as the Federal Reserve Act and amendments expressly restrict the activities of such banks.

The status of national banks, State banks and trust companies is definitely fixed by the terms of the Act.

The regulations of the Board are made pursuant to the provisions of the Federal Reserve Act and are intended to provide the necessary method of procedure to carry into effect what Congress has enacted just as the regulations of the Comptroller have heretofore been made pursuant to the provisions of the National Bank Act.

7/20/16.

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Washington, D. C., July 20, 1916.

MEMORANDUM FOR THE BOARD SUBMITTED THROUGH COUNSEL'S OFFICE

By Breckinridge Jones.

One prime objection on the part of State banks and trust companies to becoming member banks is while a national bank has its rights fixed by Federal statutes and a change can come only by an Act of Congress, a State bank or trust company becoming a member bank is subject to the discretion of the Federal Reserve Board as expressed from time to time in rules and regulations passed by the Federal Reserve Board.

It appears that under the construction placed by the Federal Reserve Board on the Reserve Act this latter statement is true. It seems clear that under the circulars relating to the admission of State banks and trust companies issued by the Board the Board has so construed the Act. The result is that State banks and trust companies have found this one of the main causes that has led them to refrain from becoming member banks - the fear being that the State institution might be deprived of some of its charter powers.

A trust company might come in under rules and regulations that do not deprive it of some of its charter powers; and, yet being in, if, the Board has the power to make such rules and regulations subsequent changes might be made so as to so restrict the trust company operations as to deprive it of an essential part of its business.

This objection is fundamental.

When a State bank or trust company becomes a member bank its status and rights, so far as the Federal Reserve Act is concerned, should be as crystallized and definite as are those of the national bank - that is, to be subject to change only by an Act of Congress.

My contention is that this is true under the Federal Reserve Act and that a contrary view has obtained only because of error on the part of the Federal Reserve Board in construing the Federal Reserve Act.

Under the National Bank Act and the Federal Reserve Act the status and rights of a national bank are clearly set out yet thereunder the Comptroller has the right to make "rules and regulations" but these relate only to the modus operandi

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and are administrative only in their features.

So I contend that the Federal Reserve Act expressly fixes the requirements to be met by a State bank or trust company in being admitted as a member bank and the right of the Federal Reserve Board to make rules and regulations was intended by Congress to relate only to the modus operandi, or merely to be administrative features.

(A brief on this subject was filed by me with the Federal Reserve Board some months ago and copy of it is handed herewith to Judge Elliott)

My plea is that the Board pass a resolution adopting this construction of the Federal Reserve Act. If it will do so then the subsequent changes in the circulars and forms relating to the admission of State banks and trust companies as heretofore issued by the Board become matters of detail easily made to harmonize.

There is nothing in this suggestion tending to weaken the Reserve System or to impair the right of examination and supervision on the part of the Board.

If a State bank applies to become a national bank the Comptroller has the power to examine and see that the bank is sound and if it is admitted as a national bank the Comptroller has ample power under his rules and regulations to see that it obeys the laws of its being. So when a State bank or trust company applies to become a member bank the Federal Reserve Board, through its proper agencies, has power to examine and see that the applying institution is sound, and if it is admitted the Board has ample power to see that it remains sound and that it obeys the laws of its being.

But some one objects. Suppose a bank or trust company has under its charter the right to do certain kinds of business not ordinarily incidents of banking?
For example -

(1) Acting as executor or administrator.
(2) Becoming surety on the bond of an individual acting in such capacity.
(3) Insuring lives and granting annuities.
(4) Doing a farm loan business.
(5) Issuing debentures against real estate loans.
(6) Buying, selling and investing in bonds, stocks, and other investment securities, etc., etc.

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My answer is that when Congress expressly provided for State banks and trust companies, when incorporated under general laws or special charters, coming into the System under the express limitations set out in the Act, it had in view that such State institutions were different from national banks, having powers beyond the powers of national banks.

Moreover, what difference does it make to the Federal Reserve Board what powers the States have given these institutions so long as the Board has ample power to see that these institutions are safe and sound and comply with the laws of their being. If they come in they must buy stock in a regional bank, must keep reserve there, and can get Federal reserve notes only to the extent that they have paper eligible for discount.

As a practical conclusion, unless a State bank or trust company has business of a kind that will enable it to avail itself of the benefits of the Reserve System it will not ask to come in.

One of the provisions of the Federal Reserve Act is objected to by nearly every national bank and has been and is a prime cause in keeping out of the System State banks and trust companies.

I refer to Section 22.

The objections to that Section have been urged so often by so many that I need not repeat them. Judge Elliott is familiar with them.

It is not difficult to suggest an amendment that will fairly answer objections and yet leave the Section effective to prevent the faults hit at by its authors. Judge Elliott has the form of such an amendment.

It would be easy to get hundreds of petitions for this change but such a public campaign would be unwise at this time. The Currency Committees in the Senate and House would readily understand the proposition. If the amendment could be recommended by the Board and put through this session of Congress and the Board would construe the Act as indicated in the first paragraph of this memorandum, I believe a large number of State banks and trust companies would promptly come into the System, and the popularity of the System would be established.

BRECKINRIDGE JONES.

7/24/16.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 24, 1916.

My dear Mr.

Mr. C. H. Bosworth, Chairman of the Federal Reserve Agents' Committee on Publicity, has sent a copy of his report for the information of the Federal Reserve Board. The report is so interesting that we have had it mimeographed for the benefit of the Board; and I am also sending you three copies for such use as you may desire to make of them.

Yours very truly,

Vice Governor.

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July 21, 1916.

ORDER NO. 9808

Departmental Order of July 19, 1916, appearing in the Daily Bulletin of July 20, 1916, is extended so as to provide that the Third Assistant Postmaster General, on request of the Federal Reserve Board, may designate the post offices at which collections are to be made for Federal Reserve Banks of checks drawn on non-member banks, and shall furnish definite and detailed instructions at the time the designation is made. Postmasters must refrain from making these collections until their post offices are designated for the purpose.

(signed) A. S. BURLESON

Postmaster General.

7/24/16

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NOTICE TO ALL POSTMASTERS.

July 24, 1916.

The Chairman of the Federal Reserve Board has transmitted to this Department the following letter, dated July 18, 1916:

"I have the honor to give below copy of a resolution today adopted by the Federal Reserve Board, as follows:

WHEREAS, it is necessary and desirable to facilitate the collection of checks presented through member banks but drawn on non-member banks, especially in cities and towns where there may be no member banks to act as collection agencies; now therefore be it

RESOLVED, that the Honorable Secretary of the Treasury, Chairman of this Board, be officially requested to present to the Honorable Postmaster General the desire that the Honorable Postmaster General shall authorize postmasters to receive checks from Federal Reserve Banks drawn upon State banks non-members of the Federal Reserve System; that they be requested to collect these checks in currency and remit the currency to the Federal Reserve Bank by registered mail; the Federal Reserve Bank of the District to pay all expenses for postage and registration fees upon funds thus remitted.

As you know, the clearing and collection plan, covering the country-wide collection of checks at par by Federal Reserve Banks, went into effect on July 15, 1916. The request contained in the resolution is intended to enable the Federal Reserve Board to make use of postmasters for the presentation of checks at the counters of banks which refuse to remit to Federal Reserve Banks. It is desired that, having received payment of these checks, the postmasters remit the proceeds to the Federal Reserve Bank of the district. While it is not anticipated that it will be necessary to make use of this expedient to any wide extent, the permission so to do is much desired by the Board as a part of its clearing and collection plan. It will be necessary only in towns or cities where there is no member bank of the System to make the collection."

Postmasters are authorized to receive checks from Federal Reserve Banks drawn upon State banks non-members of the Federal Reserve System and they must comply promptly with requests of the Federal Reserve Bank of your District to collect these checks in currency and to remit the currency to the Federal Reserve Bank by registered mail.

A. S. BURLESON,

Postmaster General.

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754-a

July 27, 1916.

MEMORANDUM FOR MR. DELANO:

Subject: Clearing Statistics.

Statistics are desired which will show both the number and amount of items handled by each Federal reserve bank, subdivided as follows:

1. Local Federal reserve city (C. H.) items on member and non-member banks:

2. Items on member and non-member banks within the district, outside the Federal reserve city:

3. Items sent to another Federal reserve bank on member and non-member banks:

4. Items sent direct to member or non-member bank outside the Federal reserve district without the intermediation of another Federal reserve bank.

If it is desired to compile statistics of Federal reserve bank clearings in all the 12 districts, group 3 should be eliminated, since all items composing this group are also shown in groups 1 and 2.

For the present, in order to save expense, it is not proposed to obtain data showing separately items on member and non-member banks, though information along these lines, if readily available, should be of interest to the Board.

Respectfully submitted,

M. JACOBSON
Statistician.

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Copy of reply made by the Federal Reserve Board to a letter received from a national banker in regard to Circular of July 22d, 1916, sent out by the "Conference of Bankers."

July 25, 1916.

Referring to your letter of the 25th instant addressed to Governor Hamlin, inclosing copy of a circular letter dated July 22d from the "Conference of Bankers", I beg to advise that the committee referred to was not justified in stating that a proposed suit to test the authority of the Board to put into effect the clearing system is regarded in an entirely friendly light by the Federal Reserve Board. On the contrary the Board is decidedly of the opinion that the establishment of a scientific clearing system should have the cooperation and support of all conservatively-managed banks. The defects of the many independent clearing systems heretofore in force are so well known that a discussion of them is unnecessary.

While the Secretary of the committee was informed that the courts were, of course, open to them, if they felt that the action of the Board worked any injustice, the suggestion was made that they might file a frank and full statement of their position with the Board and ask for some definite remedy.

The Board has acted in this matter only after due deliberation and is in no sense apprehensive as to the legality of its action. It, therefore, does not feel that any necessity exists for bringing a suit to test the question involved and any statement that the Board looks with favor upon litigation of this sort is unwarranted.

7/28/16

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SECRETARY OF THE TREASURY
CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 28, 1916.

Dear Sir:

With the view of insuring the use of more uniform methods in figuring average rates of earnings for the several classes of earning assets held by the Federal reserve banks, I take the liberty of inclosing 25 copies of a somewhat enlarged form (No. 722) which I would ask you to use in place of the old form furnished sometime ago.

You will note that we have added three columns headed respectively:

(2)	(3)	(4)
Total of daily holdings for the month as shown on Form 34.	Transit items. Amounts purchased for bank's account multiplied by number of days intervening between date of purchase and date of entry on books.	Aggregate of (2) & (3)

It is hoped that your bookkeeping department will use the utmost care in reporting earning assets for a number of days corresponding to the number for which earnings are shown, and that the earnings for the transit period will be credited upon receipt of advice from the purchasing bank, and not be spread over the period during which the investment is actually held by the bank. The following example will illustrate what is meant by corresponding number of days:

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Suppose that an acceptance or warrant was purchased by the New York Federal Reserve Bank for one of the western banks. New York immediately notifies the western bank by mail of the purchase. The notice is received by the western bank three days later, The bank then enters on its books the discount or interest for the three days which the acceptance or warrant has run. As there can be no corresponding entry against the amount of acceptances or warrants held, Form 34 having already been forwarded to the Federal Reserve Board, it is necessary for the purchasing bank to set up in column (3) of enclosed Form No. 722 for reporting the annual rates of earnings, the amount of the purchase multiplied by the number of days in transit. This will result in having the earning assets held and the earnings therefrom appear for an equal number of days.

In figuring average holdings for the month, it is very desirable that you use the actual number of days (and not an average of 30 days for each month), likewise in figuring the annual rate of earnings that you use the actual number of days in the current year (i. e., 366 days for the present year).

Earnings should be given in full, i. e., for the entire number of days in the month for which the investment has run, including the days in transit. Earnings for the transit period should not be credited to "Sundry Profits".

Very truly yours,

Assistant Secretary.

Enclosure:

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 28, 1916.

Dear Sir:

Referring to letters of instruction under dates of July 21 and 24 in regard to collection of chekcs of non-member banks through postmasters:

Certain questions have arisen as to the form of bond to be given, or blanket policy to be issued and the Board has therefore concluded to request that no arrangements be made for the collection of checks through postmasters until some uniform scheme of bond or insurance for such transactions shall have been perfected.

You are therefore requested to take the matter up and report to the Committee on Clearing of the Board your recommendations as to the best manner of handling this proposition. In order that the matter may be handled in a uniform way, it may be desirable to appoint a Committee to represent all of the Federal reserve banks and if you desire to handle it in this manner you are authorized to so arrange.

Respectfully,

Governor.

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Released for publication July 30, 1916.

STATEMENT FOR THE PRESS.

The attention of the Federal Reserve Board has been called to the fact that a circular dated July 22, 1916, and signed by T. H. Dickson, as Secretary of the conference of bankers held at St. Louis, contains the following paragraph:

> "The administrative committee has decided to bring suit seeking to set aside the Federal Reserve Board's order of May 1st on the general grounds herein outlined. The committee understands upon good authority that the proposed suit is regarded by the Federal Reserve Board in an entirely friendly light".

The order referred to is manifestly Circular No. 1, Series of 1916, which relates to the collection and clearance of checks.

The Board recognizes the right of any member bank to resort to the courts to test the constitutionality of any provision of the Federal Reserve Act; to procure the court's interpretation of any part of the Act; or to question the legality of any regulation of the Board. Where such a course is necessary to remove any doubt that may exist the Counsel for the Board will cooperate as far as possible in expediting a hearing in order that the banks and the Board may have the benefit of a judicial determination of the question involved.

The statement contained in the circular above referred to that the proposed suit is regarded by the Federal Reserve Board in an entirely friendly light might lead to the conclusion that the Board is in doubt as to its power to promulgate the regulation in question and, therefore, welcomes litigation designed to settle the question. The fact that such an impression may be created by the circular is evidenced by inquiries received from some of the banks as to the attitude of the Board. This statement is, therefore, misleading. The regulation in question was adopted after deliberate consideration and is intended to carry out one of the important purposes of the Act, namely, the substitution of one compact clearing system for the many independent collection organizations heretofore in force.

The Board has not been informed of the character or form of procedure it is proposed to adopt in order to set aside the regulation of May 1st. If any of the member banks feel aggrieved at this regulation and desire to resort to the courts there is, of course, no disposition on the part of the Board to interpose any objection to any action they may deem it proper to take. It desires, however, to correct any impression that may have been created that the proposed litigation is a "friendly suit" in the sense that this language is ordinarily used, namely, a suit to determine some question about which the parties involved are mutually in doubt.

July 29, 1916.

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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
761.
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

August 2, 1916.

Dear Sir:

There have been received many inquiries relating to applications for consent of the Federal Reserve Board under the Kern amendment to the Clayton Act.

The Federal Reserve Board desires each applicant to make on the reverse side of Form 94 a complete list of all firms of which he is a member and a complete list of all corporations of which he is a director, officer or employee.

Inquiries about the questions which banks are requested to answer on Form 94 will be taken up in proper order.

Question No. 1. Character of the community which the banking institution serves.

The answer to this question should state the character of business of the community or in case of a large city of that section from which the bank draws a large majority of its customers.

Question No. 2. Character of business of the institution.

The reply "Commercial banking" would be sufficient if bank did not engage in other banking activities.

Question No. 3. Describe nature of demand deposits.

The answer should state whether bank, commercial, or individual, whether checking accounts or demand certificates of deposit, whether the average deposit is large or small and whether interest is allowed.

Question No. 4. Describe nature of time deposits.

This means whether saving accounts or time certificates and also character of depositors and approximate average size of deposits.

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Question No. 5. Describe nature of acceptance liabilities.

A reply stating the liabilities on commercial letters of credit covering exports or imports and domestic transactions and location of the bulk of the customers for whom credits are opened would be sufficient unless the bank issued cash letters of credit, travelers' checks, etc.

Question No. 6. State practice of bank in respect to purchasing commercial paper, e. g. continuous or seasonal.

The reply "continuous" or "seasonal", as the case might be, would be sufficient. It might be well to mention in which markets purchases are primarily made.

Question No. 8. Describe nature of collateral.

This means the character of the collateral, i. e., commercial paper, stocks, bonds, mortgage notes, etc.

Question No. 9. Describe character of investments.

A reply stating "Long and short term railroad and municipal bonds and notes" would be sufficient, unless the bank made investments in real estate securities, etc.

Question No. 10. Describe practice of bank in respect to acquiring and disposing of investment securities.

Answer should state whether the purchases and sales are made in the open market or directly from corporations, etc., and whether underwriting syndicates are joined or formed, whether securities are acquired for long time investment or for short time investment for resale to customers, etc., and also whether there is a bond department.

Question No. 11. Describe nature of foreign exchange business, if any, done by the bank.

Reply should indicate amount of the business, with what foreign countries, whether or not done direct or through other institutions and whether only for customers or a wide open-market business.

Question No. 12. Describe kind and extent of fiduciary business done by the bank.

This includes acting as registrar of stocks and bonds, looking up and guaranteeing titles, etc.

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While in cases which are clear, the Board does not desire to be technical in passing upon the sufficiency of the answers to the questions on Form 94a, it will be necessary for the replies to go more into detail in the doubtful cases and in dealing with these the Federal Reserve Agent should use his own discretion in getting at all facts. The questions outlined in the schedule are only to be considered as general leaders.

Information relating to the ownership or control of the institutions involved would be very helpful in determining the question of substantial competition. Where the same group of individuals control the boards of directors of two banks the test should be whether the banks would, under normal conditions, be in substantial competition on October 15, 1916, i. e. on a date when the control no longer exists.

Where a group of persons owns the majority of the stock in two banks and through such ownership controls both institutions, careful consideration should be given to the question of whether the public is deprived of the benefits of competition by such control, and whether under normal conditions substantial competition would exist between the two institutions. Conditions of that kind, if found, should be considered as tantamount to substantial competition.

Very truly yours,

Governor.

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1452

Confidential. 770

SCHEDULE OF CONVERSIONS OF 2% BONDS FOR 3% CONVERSION BONDS AND ONE YEAR TREASURY NOTES OCTOBER 1, 1916.

BANK.	Total allotment for 1916 as apportioned by Fed.Res. Board.	Converted April 1, 1916.	Converted July 1, 1916,	Total conversions to date.	Balance allotment for 1916.	Issues that may be approved Oct. 1, 1916. Bonds	Notes
Boston.....	$2,763,900	$ 500,000	$	$ 500,000	$2,263,900	$1,132,900	$1,131,000
New York.....	6,130,500	3,065,300	1,500,000	4,565,300	1,565,200	783,200	782,000
Philadelphia.....	2,849,100	1,424,600	712,200	2,136,800	712,300	356,300	356,000
Cleveland.....	3,249,600	400,000	2,000,000	2,400,000	849,600	425,600	424,000
Richmond.....	1,827,600	913,800	456,900	1,370,700	456,900	228,900	228,000
Atlanta.....	1,410,600	705,300	352,600	1,057,900	352,700	176,700	176,000
Chicago.....	3,635,400	1,000,000	1,700,000	2,700,000	935,400	469,400	467,000
St.Louis.....	1,523,400	761,700	380,800	1,142,500	380,900	190,900	190,000
Minneapolis.....	1,398,600	699,300		699,300	699,300	350,300	349,000
Kansas City.....	1,644,000	820,600	412,400	1,233,000	411,000	206,000	205,000
Dallas.....	1,412,400		1,059,300	1,059,300	353,100	177,100	176,000
San Francisco....	2,154,900		1,000,000	1,000,000	1,154,900	577,900	577,000
Total	30,000,000	10,290,600	9,574,200	19,864,800	10,135,200	5,074,200	5,061,000

Prepared by:
Division of Loans and Currency,
Treasury Department.

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772
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

August 15, 1916.

Dear Sir:

Conversions of two per cent bonds into 30-year three per cent Conversion bonds and one-year three per cent Treasury notes for the current year will be completed on October 1st.

There is inclosed for your information a statement showing the bonds already converted, the balance of the allotment for 1916, and the division of this remaining allotment in bonds and notes.

Under the previous announcements made by the Board, if any Federal reserve bank concludes not to apply for its full allotment prior to October 1st, the bonds and notes remaining will be distributed pro rata among the banks applying for more than the amounts which they would otherwise receive. Will you, therefore, advise the Treasury Department, Division of Loans and Currency, to reach Washington not later than September 15th, whether you desire to take your full allotment of bonds and notes, and if you desire an additional allotment should any bank decide not to take the full amount of the allotment to which it is entitled. Please advise the Board of the action which you are taking in the matter at the same time.

Very truly yours,

Governor.

Inclosure.

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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PAUL M. WARBURG, VICE GOVERNOR
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ADOLPH C. MILLER
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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

782

August 28, 1916.

Dear Sir:

The Committee on Clearing of the Federal Reserve Board desires information as to the number of important cities in the country which have modified their clearing house rules as a result of the new method of check clearing and collection. May we therefore ask you to prepare a list of reserve and other cities in your district having clearing house associations, stating as briefly as possible whether they have modified their rules and what their present collection charges are.

Your early attention to this matter will oblige

Yours very truly,

Chairman of Committee on Clearing.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

489

September 8, 1916.

Dear Sir:

Amendments to the Federal Reserve Act, as printed in the September number of the Federal Reserve Bulletin, were signed by the President on September 7th and are, therefore, law.

In this connection your attention is called to the fact that the following words, comprising the last six lines of the second paragraph on Page 440 of the Bulletin were through error omitted by the Conference Committee:

> "except by authority of the Federal Reserve Board, under such general regulations as said Board may prescribe, but not to exceed the capital stock and surplus of such bank, and such regulations shall apply to all banks alike, regardless of the amount of capital stock and surplus."

The Board discovered the omission when the Bill was referred to it for approval and although effort was made it was found impossible to correct the mistake during the closing hours of Congress. The matter will, therefore, be left in abeyance until Congress reconvenes in December when there is every reason to hope and believe that the correction will be made.

Pending such correction the Federal Reserve Board will be unable to grant any new requests from member banks for permission to accept to 100%, under the powers above quoted.

Very truly yours,

Governor.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

September 11, 1916.

Dear Sir:

This will remind you that copy covering business conditions for the Federal Reserve Bulletin, to be issued on the first of next month, will be welcome in the office of the Federal Reserve Board not later than the 23rd of this month. Its prompt receipt will aid in getting the Bulletin out on time.

In sending this copy will you also include data similar to that found on page 445 of the Federal Reserve Bulletin for September, on which a statement can be prepared as to the operation of the clearing plan.

There have been sent you slips on which the Board requests that you fill in briefly answers to the questions covering conditions in general business, crops, bank clearings, and other indications of general trend. Please return one of these slips with each report of business conditions. They are desired for the purpose of making an accurate summary of conditions in the United States.

Very truly yours,

Governor.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

791

September 9, 1916.

Dear Sir:

With the view of securing for the Federal Reserve Board accurate and detailed information regarding the expenses of operating the transit department of your bank may I request that you state on Form 287 - b, in detail, against the respective captions, these expenses separately for the period July 15 to July 31, and August 1 to August 31.

Will you also be good enough to inform us how the expenses of your transit department for the above periods were carried in your monthly statements on Forms 286 - 287 b, particularly whether the expense has been included among the operating expenses of the bank for July and August.

The Philadelphia and Atlanta banks report the transfer to the account of the transit department of certain operating expenses incurred prior to July 15, in addition to the transfer of certain amounts under the head of "Cost of Furniture and Equipment."

It will be of some help to us if you will kindly send us complete data under these two heads, so our Statistical Division may be able to compile a comparative statement showing both initial cost and operating expenses of the transit departments of all the twelve banks.

You will greatly oblige us by furnishing us with the above data at the earliest practicable date.

Very truly yours,

Governor.

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AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

September 11, 1916.

S i r :

Inasmuch as the term of office of one Class "A" director and one Class "B" director of your bank will expire on December 31, 1916, arrangements should be made to hold an election of directors to succeed those whose terms expire, such new directors to serve for terms of three years each.

The Board has fixed November 21st as the date for opening the polls. You should accordingly arrange to have printed:

(a) Certificate of election of District Reserve Elector.

(b) Certificate of nomination for Class "A" Director.

(c) Certificate of nomination for Class "B" Director.

These certificates, as printed last year, contain form of resolution to be adopted by the member banks. A sufficient number should be prepared and mailed to each member bank in the group which elected the director whose term expires on December 31, 1916. It will be necessary, therefore, for you, as Chairman of the Board, to group the banks in your District in accordance with the Act, following the general lines of the plan set forth in the circular of the Organization Committee. When these certificates have been returned by the banks the electors should be listed and the preferential ballot prepared.

Under the provisions of Section 4, this ballot need not show the name of the bank placing in nomination any candidate, but if not on the ballot a separate list should be prepared showing by whom each candidate is nominated. If this is done, the ballot form used will be somewhat simplified, since the voting columns, showing the first, second and third choice of the elector, can appear on the same page as the name of the candidate.

Section 4 of the Federal Reserve Act provides that:

"Every elector shall within 15 days after the receipt of the said list certify to the Chairman his first, second and other choices.

The polls for the election of directors would, therefore, close fifteen days after November 21st, and in consequence, arrangements should be made to have the ballots in the hands of the electors not later than November 21st.

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Very truly yours,

Governor.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

September 11, 1916.

Dear Sir:

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

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

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

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

Very truly yours,

Governor.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

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September 11, 1916.

Dear Sir:

The recent amendments to the Federal Reserve Act provide in part that the Federal Reserve Board shall have power "by general ruling covering all districts alike, to permit member banks to carry in the Federal reserve banks of their respective districts any portion of their reserves now required by Section 19 of this Act to be held in their own vaults."

In pursuance of the authority vested in it by this Section the Board hereby rules that, effective September 18, 1916, and until further notice, any member bank so desiring shall be permitted to carry in the Federal reserve bank of its district any portion of its reserves now required by law to be held in its own vaults.

Please inform the officers of your bank that they may advise the member banks of your district.

Very truly yours,

Governor.

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AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

September 11, 1916.

Mr. M. B. Wellborn,
Chairman of the Board,
Federal Reserve Bank,
Atlanta, Ga.

S i r :

The Board has received a letter signed by Cashier Bell, dated September 7th, in which he confirms your code telegram instructing the withdrawal from the gold settlement fund of $1,000,000 and the deposit of same amount with the Treasurer of the United States for your bank's credit. Mr. Bell states that the object in having this deposit made was to provide for the shipment to your bank by the Treasurer of the United States of the same amount in gold certificates and United States notes of small denominations, enabling you to supply the demand which you anticipate will be made upon you by member banks, and he goes on to say that he may have occasion to make similar requests in the future. Mr. Bell further states that you prefer, "for the time being at least, to put in circulation in our district United States currency which we can obtain at a cost to ourselves of approximately 20¢ per thousand rather than issue our notes at a considerably greater expense to us."

While the Board recognizes the importance of small economies in the operation and administration of the Federal Reserve Banks, it feels, nevertheless, that it is unwise to lose sight of the larger objects to be attained. It is of the opinion that it is highly desirable that there be held in the vaults of the Federal

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Reserve Banks of the United States Treasury and Sub-treasuries as large an amount of gold as possible, and it deprecates the use of gold certificates and legal tender notes for crop moving purposes. Silver certificates in small denominations and national bank notes will naturally form a substantial part of the circulating medium, but the Board would prefer to have Federal Reserve notes used wherever possible, and is anxious to see this policy adopted by the Federal Reserve Banks. It hopes, therefore, that your bank will not let a desire to save a small expense influence it in this respect and that whenever it can issue Federal Reserve notes it will do so, thereby helping to concentrate gold certificates in the vaults of the Federal Reserve Banks and to put in circulation currency of an elastic character, which will be withdrawn automatically as soon as the demand for it ceases.

Very truly yours,

(Signed) W. P G. HARDING.

Governor.

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Washington, December 9, 1916.

DRAFT OF PROPOSED RATES FOR COLLECTION CHARGES ON CHECKS.

1. Section 16 of the Federal Reserve Act provides in part that:

> "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."

2. In accordance with the above provision of the Act and in compliance with various and sundry requests of patrons of the banks the Federal Reserve Board has established the following rules and scale of charges to be effective as between Federal Reserve Banks and their member banks and as between member banks and their patrons, or customers; said rules to become effective on and after 1917.

3. Federal Reserve Banks will charge their member banks for the collection of items on the basis of crediting items on a time schedule not to exceed one-half cent per item, or per check, for all items drawn against member banks.

4. Federal Reserve Banks will charge their member banks for the collection of items drawn against nonmember banks agreeing to remit at par, which items shall be credited as heretofore explained, not to exceed one and one-half cents per item.

5. Federal Reserve Banks will charge their member banks for the collection of items drawn against nonmember banks declining to remit at par 5¢ per item and $1.00 per $100 gross of items and credit the items in the manner heretofore explained.

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6. Member banks will be authorized to act for any Federal Reserve Bank as collecting agencies for State nonmember bank items, except in Federal Reserve Cities or in cities where a Federal Reserve Bank has established a branch or an agency. In such cases Federal Reserve Banks may pay for the service rendered by member banks in collecting such nonmember bank items as may be sent to them for collection an amount not exceeding 3¢ per item and 25¢ per one thousand dollars gross.

7. Member banks may charge their patrons, or customers, upon items drawn on other member banks a collection charge not exceeding 1¢ per item and on checks drawn upon assenting nonmember banks a collection charge not exceeding 3¢ per item, and on banks refusing to remit at par 6¢ per item. In addition to the above collection charge member banks may make an interest charge at the rate of 4½% per annum if the depositor or customer of the bank desires that the face value of checks be made immediately available in the form of cash or as a deposit drawing interest or subject to check without allowing time for collection. If, however, the depositor of out of town checks accepts credit deferred on the basis of the member bank's collection schedule no charge in excess of the collection charges already authorized shall be made.

8. Member banks will not be authorized to give more favorable terms to some depositors than to others, unless and until the proposed terms shall have been submitted to the Federal Reserve Board and approved by it.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

December 9, 1916.

Dear Sir:

At the meeting of Federal reserve agents in Washington this week there was discussion of the quantity of Federal reserve notes which should be kept on hand in Washington or at subtreasuries as a reserve stock for each Federal reserve bank. No detailed recommendation by individual agents of the amount in their judgment necessary to provide for present and future requirements of the banks was submitted.

The Committee on Issue and Redemption, acting for the Board, desires the matter again to be brought to your attention and requests that you will consider the question and advise the Board, to reach Washington not later than December 15th, as to the following:

1. The amount of notes, by denominations, which you have now on hand.

2. The amount of Federal reserve notes of each denomination which you believe should be maintained for your bank in the bank vaults, or if the bank is located in a subtreasury city, in the subtreasury.

3. The amount of notes in each denomination, if if any, which you desire to have maintained as reserve supply in the nearest subtreasury.

4. The amount of notes of each denomination which you desire to have maintained, in addition to the above, in Washington.

It is the purpose of the Committee to obtain your recommendation and upon it to work out a minimum note supply to be as nearly as possible automatically maintained.

Very truly yours,

Secretary.

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No. 800

Release at Noon,
Sept. 29, 1916.

Summary of address of
Hon. Paul M. Warburg,
Before Convention of
American Bankers' Association,
Kansas City, Mo., Sept. 29, 1916.

FUTURE OF THE FEDERAL RESERVE SYSTEM.

Changes Urged by Paul M. Warburg.

Kansas City, Mo., Sept. 29. The Federal Reserve Act has met many currency and banking problems with the greatest success and represents one of the greatest contributions ever made by Congress. But we must not stand still - and further development is necessary in a number of important respects, Paul M. Warburg, member of the Federal Reserve Board, impressed upon the American Bankers' Association today. Without this, he warned, the United States cannot hope to rise to the fullest measure of its financial and commercial opportunities created by the new world conditions.

Part of the two billions of gold needlessly and wastefully scattered all over the country, unmobilized and inert, must be mobilized and rendered effective as reserve, he declared. He explained how this could be accomplished without disturbance, and presented detailed analytical figures to prove that the desired steps could be taken without danger of "inflation," a bugaboo that had frightened some superficial critics.

Mr. Warburg also submitted reasons why there ought to be vital readjustment of the relations of the Treasury and the

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Comptroller's office towards the Board and its administration of the nation's monetary system.

"The Federal Reserve System, in its present form, is not a finality but a beginning," he said, "and should be improved as experience dictates". "Indeed," Mr. Warburg added, "the Federal Reserve Act would prove a failure if changes in the system did not become necessary from time to time."

The theory that notes may not be issued by the Federal Reserve Banks against gold without a certain reserve of commercial paper "makes all Europe laugh at us" and should be discarded, he showed.

Having described deposit banking as "the art of wisely employing the depositors' stored up purchasing power," Mr. Warburg said: "The Federal Reserve Act created a system of twelve central banks which, co-operating with one another, were from then on to exercise two important functions in relation to their member banks; first, to provide a sufficient gold cover for the country's gold obligations; and, second, to provide the machinery for turning, whenever desired, the member banks' commercial assets into available credit balances or cash.

"The law, however, continued the anomaly of requiring member banks to lock up in their vaults hundreds of millions

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of dollars, thus preventing them by legal enactment from giving additional strength to their own protective system, even if they should want to do so. It further created the anomalous situation that, while a balance with a Federal Reserve Bank could be considered as reserve, the Federal Reserve note could not be so counted despite the fact that it is a prior lien against the assets of the bank, and is the obligation of the United States, while the balance is not.

"This inconsistency - to a certain extent at least - has been cured, Congress having passed, upon the recommendation of the Board, a most important amendment authorizing the Board to permit member banks to keep any portion of their required vault reserve as balances with their Federal Reserve Bank. In passing this amendment, Congress has opened the path for great strides in advance, and it remains to be seen now, how far the bankers of the United States will be able to seize this opportunity of doubling the strength of their Federal Reserve Banks.

"Let us, in our plans for the future, try to look at the problem as a simple question of keeping a sufficient balance with the Federal Reserve Bank, and when that is maintained, leave it to the member bank to keep liquid and strong in its own way. Do not let us apply the term 'reserve' to a balance with another member bank, which may be invested in securities, or loaned on the stock exchange; nor let us count

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as reserve checks in process of collection, and yet, at the same time, treat Federal Reserve notes as an asset that cannot be counted as a banking reserve.

"What is the Federal Reserve System's lending power today? If we set aside a gold reserve of only 40% - which may do in times of stress, but it is not a proper and sufficient basis in normal times - we find that we have a free gold reserve of about $206,000,000, or, if we include the gold now held in cold storage by the Federal Reserve Agents, about $380,000,000. This means that, by additional rediscount operations, or purchases in the open market, for home requirements or for export, we are able to stand a loss of gold from two to three hundred million dollars. $200,000,000 is a very large amount, but when we realize that the nation's gold holding in one year has increased by about $500,000,000, it is well for us to consider whether or not we shall be able to hold this gold at the end of the war.

It is impossible to predict what will then be our economic and financial situation. Perhaps we may find ourselves in an over-expanded or generally unsatisfactory condition, and we may have to face a readjustment in which all our banking strength may be required. On the other hand, things may go well with us, but in the rest of the world there may be a great deal of financial distress.

"In that case (and it may be the more likely of the two)

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we shall have almost boundless opportunities, but serious obligations as well. Foreign loans in the old and the new world may draw away our capital at interest rates far in excess of our own. Our exporters will have to meet the keen competition of other nations, and even though at first there will probably be a strong demand for certain of our raw materials, the purchasing power of many a country will be found materially reduced. These are conditions which, in the long run, may be the cause of heavy gold exports from the United States and which, if we remain unprepared, may seriously check our progress. If, on the other hand, we forearm, we may grasp the opportunity of taking our place as the strongest of the world's bankers and furnish our industries with the basis for a solid expansion.

"Does it not appear ridiculous that a country owning over two billions and a half of gold should not be able to mobilize a larger free gold reserve than two or three hundred millions of dollars - particularly when it is apparent that its future financial and economic growth will depend upon the extent of the 'preparedness' that it can provide in this respect?

"During the critical period following the outbreak of the war in 1914, there were issued $386,000,000 of currency under the so-called Aldrich-Vreeland Act. Has it occurred to you that if a similar amount were needed under the Federal Reserve Act, it would absorb a gold reserve, on a 40% basis, of $154,000,000? But financial history has shown that each

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crisis develops larger demands than its predecessor, and, with our constantly growing pyramid of deposits and loans, and with the gigantic scale upon which financial transactions are now conducted, it is our duty to be prepared for ever larger demands. The fact that we are strongly forearmed, far beyond a limit expected to be actually reached, will be the only means of restraining these demands to safe and reasonable bounds. We ought to be able, therefore, to lose $300,000,000 to $500,000,000 and still have $200,000,000 or $300,000,000 of free gold to serve as a basis for emergency operations.

"I cannot urge you too strongly, therefore, to co-operate to the utmost of your abilities in keeping your balances with the Federal Reserve Banks high, and your vault money down to the minimum that your own till requirements will safely and conveniently permit. It is obvious that, in strengthening the Federal Reserve Banks, you are strengthening yourselves."

Having compared European banking systems with ours, Mr. Warburg added: "The bank of England issues notes only against gold. The other leading central banks of Europe issue notes against gold (in certain countries, gold and silver) and commercial paper. There may be 100% of gold, but there may not be less than a prescribed minimum gold reserve. But they do not provide that notes may <u>not</u> be issued against gold without a certain reserve of commercial paper. That theory,

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however, is the one underlying the Federal Reserve Act. The Board urged Congress to remedy the law in this respect. The Senate responded favorably by passing a bill on these lines, but, unfortunately, it was lost in conference.

"It is hard to comprehend why if this principle has been universally and successfully adopted by the leading central banks, and has been the root of their surprising strength during these last two years of terrific strain, it should be arbitrarily condemned or disregarded by us."

The $700,000,000 to $750,000,000 of gold certificates and gold, in addition to other kinds of currency, at present carried in the pockets of the people and in business tills, should be gradually displaced by Federal Reserve notes, Mr. Warburg contended, thus mobilizing and bringing under control gold resources now scattered and more or less impotent.

The exchange of a $10 Federal Reserve note for a $10 gold certificate would not, as some writers argued, cause an increase in circulation or "inflation", but would strengthen the gold reserve position. We have now under control only about $500,000,000, while the country at large and the banks own about $2,000,000,000.

The $600,000,000 or more of gold which has come into the United States since the Federal Reserve Banks opened should have gone into these banks, and Federal Reserve notes issued against it, Mr. Warburg contended; but instead of strengthening the nation's centralized gold reserve, this gold has been

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allowed, because the Federal Reserve Banks' hands were tied, to drift into member banks or go into circulation.

The ultimate aim, Mr. Warburg submitted, should be the conversion of a large part of the 2 per cent Government bonds, now securing circulation, into new 3 per cent bonds, part of which gradually will be absorbed by the people; thus reducing national bank circulation, which ought to be withdrawn, and substituting therefor Federal Reserve notes covered by a far stronger gold reserve than that behind the national bank notes.

Mr. Warburg added: "We must rid our country of the confusing multiplicity of currency with which we are now afflicted, and the Treasury will have to stop issuing small denomination gold certificates. The circulating currency ought to be silver certificates in the small denominations and Federal Reserve notes. The best place for gold and gold certificates will be in the Federal Reserve Banks."

Instead of having had to pay out gold for $164,000,000 of investments the Federal Reserve Banks should have had the power to pay in Federal Reserve notes, secured by 40% gold, thus retaining the balance of about $100,000,000 gold as a potential reserve for additional note issues if needed.

Other points urged by Mr. Warburg were: Our usury laws should be modernized so that Banks, under certain conditions, should be allowed to charge interest in excess of 6 per cent in dealing with large and solvent concerns.

National banks should be granted the power to operate

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branches in cities where State laws do not prohibit State banking institutions from operating similar branches. The adoption of the Canadian or European branch bank system, however, would entail elements of excessive centralization.

"Self respect and public opinion will not permit the State institutions long to remain in a position of shirking their duty towards the nation. They will be expected to join the Federal Reserve System."

National banks should be allowed to accept commissions; as in Europe, for executing orders for the investment of funds of depositors.

"The administration of the Treasury funds within the Federal Reserve System," Mr. Warburg said, "should be subject to some control by the Board and emergency relief operations ought to be carried out through the Federal Reserve Banks and not directly through deposits with member banks by the Treasury.

"If at certain periods large payments are to be made by the member banks to the Treasury, there should be an easy adjustment by having the money withdrawn strengthen the Federal Reserve System, leaving it to the Board and the Federal Reserve Banks, by rediscounting short paper, to return to the member banks sufficient funds to re-establish the equilibrium.

"But this important function of balancing the scales ought to be the constant care of the Board, under a consistent plan of operation, and not the domain of the changing and

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arbitrary policies and views of each succeeding Secretary of the Treasury.

"In a similar way, the Board's authority and efficiency ought to be strengthened by providing that examinations and rulings by the Comptroller's office, and the compilation of banking statistics, should be carried on under the auspices of the Board.

"However the present members may have been able, by personal effort, to meet the organic defects of the law, the fact remains that, as it stands today, it places the Board half way between independence and dependence. It cannot remain long in that position. Evolution will carry it either in one direction or the other. The country will have to decide which development it desires and express itself in no uncertain voice."

Concluding, Mr. Warburg said: "I am an unqualified believer in and enthusiastic supporter of the Federal Reserve System. Its fundamental principles are sound; its benefits to the country have been immense and will become more apparent with each succeeding year. Though from the point of view of banking technique, one single central bank would have been easier to administer and, in some respects, might have been more economical and efficient, I am convinced that the undisturbed development of our financial system is better assured and that danger of business or political control is more certain to be avoided by a system of coordinated central banks. That

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the system might possibly be simplified and made stronger and more efficient by merging some of the districts, is an opinion held by many, a view which I entertained before the organization of the districts, and to which I am still wedded.

"By merging a few districts into twin districts, greater strength, greater efficiency, and cheaper operation might be secured, without changing or weakening the intimate touch now produced by the respective local organizations."

Mr. Warburg quoted Mr. Hartley Withers's recent statement:

> "America is now one of the leading powers in international finance, and on the wise and skilful use of its strength the future prosperity of the civilized world will, to a great extent, depend."

and asked: "Shall we be found wanting?" He continued: "The answer will largely depend upon you, the bankers of the United States; upon the strength you give to your Federal Reserve System and upon your contribution to the moulding of its future."

END.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

September 18, 1916.

Dear Sir:

You are advised that in the opinion of the Federal Reserve Board it is desirable that any dividends declared by Federal Reserve banks should be with a view to their payment at regular intervals, and that the books of the banks should be closed on June 30th or December 31st, as the case may be, so that each member bank may be credited with its proportion of the dividend not later than the following day. While the Board has not so far adhered to this policy strictly, having yielded to the wishes of the management of the Federal reserve banks in some instances, it concurs fully in the matter of dividend payments with the committee of Governors of the Federal reserve banks appointed at the conference of Governors held in Boston recently, and will not in the future be disposed to give its assent to dividend payments except at the appropriate time in June and December.

Please bring this to the attention of your directors at the next meeting.

Very truly yours,

Governor.

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Washington, D.C., September 19, 1916.

Federal Reserve

Sir:

A joint examination of the Gold Settlement Fund and Federal Reserve Agents' Fund at Washington authorized by the respective chairmen of Conferences of Governors and Federal Reserve Agents was made this morning as of close of business September 18, 1916.

A statement of your account together with blank reconcilement and addressed envelope is inclosed herewith.

Please compare with your records and return reconcilement, properly signed, in the inclosed envelope at your earliest convenience.

Very truly yours,

_____
Representing Federal Reserve Banks.

_____
Representing Federal Reserve Agents.

Inclosures.

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Sept. 19,1916.

STATEMENT FOR THE PRESS.
CLAYTON ACT.

The Federal Reserve Board has received a large number of applications from directors of national banks in all parts of the country, asking the consent of the Board to serve as directors of other banking institutions.

The Clayton Act, as originally enacted, prohibited directors of members banks of the Federal Reserve System, from serving as directors in other banking institutions, except in certain specific cases; the purpose of the Act being, in the language of the Judiciary Committee of the House, "to prevent as far as possible control of great aggregations of money and capital through the medium of common directors between banks and banking associations, the object being to prevent the concentration of money or its distribution through a system of interlocking directorates."

The Kern amendment to the Clayton Act provides that with the consent of the Federal Reserve Board, an officer, director or employe of a member bank may serve as officer, director, or employe of not more than two other banks if such other bank or banks are not in"substantial competition" with such member bank, In passing upon the applications, the Board has given careful consideration to the facts submitted by the applicants, and to the reports and recommendations of the Federal Reserve Agents of the respective districts.

The Board has considered each case on its own merits, but has taken the general position that the mere purchase by two banks of commercial paper in the open market, or the making of time or demand loans on collateral securities having a wide market, or the purchasing of such securities, need not necessarily or invariably be considered as indicating "substantial competition" within the meaning of the Kern Amendment. It is, however, the view of the Board that "substantial competition" must be held to exist in cases where the resources of the banks are of such magnitude, or of such character that the ability of the banks jointly to grant or to withhold credit, or otherwise to influence the conditions under which credit may be obtained, might constitute them a dominant factor in the general loan market, even though the character of the deposits carried by the institutions in question might be quite different.

In drawing the distinction in various cities, no fixed rule as to amount of assets could be applied, as different lines of demarcation had to be obs rved, suggested by the relative importance of the financial institutions involved and the character and scope of the markets in which they operate.

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The Board has up to this time passed on 679 applications; 556 favorably and 123 adversely. The following is a statement of the applications granted and denied in each Federal Reserve District :

	Granted	Denied.
Boston	35	15
New York	134	48
Philadelphia	85	9
Cleveland	101	8
Richmond	49	28
Atlanta	8	1
Chicago	44	8
St. Louis	7	2
Minneapolis	10	0
Kansas City	15	1
Dallas	0	0
San Francisco	68	3

All applications granted are, in accordance with the terms of the Korn Amendment , subject to revocation by the Federal Reserve Board.

September 19,1916.

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superseded by no. 832

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FEDERAL RESERVE BOARD

WASHINGTON

September 9, 1916.

My dear Governor:

An opinion of this office has been requested on the question of the proper interpretation to be given to the language "private banker" as used in the Clayton Act.

This language has been variously construed by the courts. Generally speaking a private banker may be defined as a person or firm, not a corporation, engaged in the business of banking without having special privileges or authority from the State or from the United States. (In re Surety Guaranty & Trust Company 121 Fed. 73, 74; People v. Doty, 80 New York, 225, 228; Perkins v. Smith, 116 New York, 441, 448; 23 N. E. 21).

It is, therefore, necessary to determine what constitutes the business of banking.

Since the Clayton Act prohibits private bankers, individuals or firms engaged in the business of banking from serving as officers or directors of member banks the purpose of the Clayton Act should be considered in defining the banking business. That is to say, it should be first determined what class of individuals or firms did Congress intend to make ineligible to serve as officers or directors of member banks when it prohibited private bankers from serving in these capacities.

The purpose of the Clayton Act, as its title implies and the context shows, was to prevent unlawful restraints and monopolies. It is obvious that no restraint or monopoly could be created by common control of the business of a private banker and that of a member bank unless the private banker engages in one or more activities engaged in by the member bank. It is accordingly necessary to analyze the business engaged in generally by member banks. In the case of Mercantile Bank v. New

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York, 121 U. S., 138, 156, it is said:

> "The business of banking, as defined by law and custom, consists in the issue of notes payable on demand, intended to circulate as money where the banks are banks of issue; in receiving deposits payable on demand; in discounting commercial paper; making loans of money on collateral security; buying and selling bills of exchange; negotiating loans, and dealing in negotiable securities issued by the Government, State and national, and municipal and other corporations."

In the case of Meadowcraft v. People, 163 Ill, 56, 65, a banker is defined as follows:

> "A banker is a dealer in capital - an intermediate party between the borrower and the lender - who borrows of one party and lends to another; and the business of banking is, among other things, the establishing of a common fund for lending money." Newark on Bank Deposits, Sec. 21; see also Curtis v. Leavitt, 15 New York 9, 167.

In the case of People v. Doty, 80 New York, 225, 228, a banker is defined as follows:

> "A banker is one who keeps a place for the traffic in money; who there receives it from others, and keeps it with his own; using the whole fund as his own, or remits it at request to other places; who repays it at the will and call of his customer; who furnishes money to others on the discount of their obligations, or on securities brought by them; and who buys and sells bills of exchange."

In the case of Oregon & W. Trust Inv. Co. v. Rathburn, 18 Fed. Cas. No. 10,555 (p. 765) it was held that where a corporation loaned only its own funds contributed by its shareholders, it was not engaged in the banking business, but as explained in the case of People

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v. Doty, where it mingles the funds of others with its own and makes loans, it would be engaged in the business of banking.

Eliminating from consideration the issue of notes to circulate as money, which is now confined to national banks and Federal reserve banks, an analysis of the foregoing cases indicates that the banking business may be said to consist primarily of receiving on deposit the funds of others and of lending or investing such funds for the benefit of the bank or banker.

The fundamental distinction between the business of a banker and that of a broker appears to be that the banker receives the funds of others under an agreement to repay such funds upon the order of the depositor, subject to the conditions of deposit, with or without interest, and lends such funds for his own benefit. A broker, on the other hand, may receive the funds of others for investment but is not entitled to the profits arising therefrom since he receives a commission for acting as the agent or broker of the owner of the funds in making the investment. In other words, the relation between the depositor and banker is that of debtor and creditor while the relation between the customer and the broker is that of principal and agent.

While it is difficult to define in precise terms a private banker within the meaning of the Clayton Act, it is obvious that Congress intended to prohibit those individuals or firms whose business come into competition with member banks from serving as officers or directors of member banks, and since private bankers were not included in the Kern Amendment it would seem to follow that private bankers who engage in the business of banking are precluded from serving as directors of member banks whether or not their competition with member banks may be said to be substantial.

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Section 3407 United States Revised Statutes, which deals with the subject of Internal Revenue, defines a bank in the following terms:

> "Every incorporated or other bank and every person, firm, or company, having a place of business where credits are opened by the deposit or collection of money or currency, subject to be paid or remitted upon draft, check, or order, or where money is advanced or loaned on stocks, bonds, bullion, bills of exchange, or promissory notes, or where stocks, bonds, bullion, bills of exchange, or promissory notes are received for discount or for sale, shall be regarded as a bank or as a banker."

This language may be said to be applicable to the present case in so far as it enumerates the activities usually engaged in by banks or bankers. It will be observed that this statute contemplates the maintenance of a place of business for engaging in the activities enumerated, and it is clearly indicated by the context that a person, firm, or corporation must make it a practice to engage in such activities before such person, firm, or corporation shall be regarded as a bank or banker within the meaning of this Act.

In defining the work "banker" as used in the Clayton Act, where the element of competition with member banks must be taken into consideration, the question of whether or not an individual or firm makes it a practice to engage in any of the enumerated activities is of even greater importance than in the case of the Revenue Act referred to. If, therefore, this definition is to be taken as a guide in the present case, it should be modified to exclude the broker or agent who merely buys or sells stocks, bonds, or other securities on commission and to make it clear that bankers within the meaning of the Clayton Act are those who seek to earn their profits from the exercise of one or more banking activities rather than from commissions paid for acting as

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broker or agent.

It is, of course, obvious that a broker may in some instances be called upon to engage in transactions which are engaged in by banks. He may find it necessary, as an incident of his business, to borrow money to the same extent as any other individual or firm, or he may be called upon to advance funds to consummate a brokerage contract. If he should make it a practice or a business to borrow money to lend to others he should probably be regarded as a private banker. Where advances are made by him, however, to cover marginal transactions as an incident only of the purchase or sale of securities on commission and he does not make it a practice to receive deposits or to borrow money to lend out at interest in other transactions, not incidental to the purchase or sale of securities on commission, he should not be treated as a private banker. In this view the definition quoted should be amended to read substantially as follows:

> "Every individual or firm, not a corporation, that has a place of business where credits are habitually opened by the deposit or collection of money or currency, subject to be paid or remitted upon draft, check, or order, or where the profits of the business engaged in are derived to an appreciable extent from money loaned or advanced on stocks, bonds, bullion, bills of exchange, or promissory notes, or where it is customary to receive bills of exchange or promissory notes for discount, or stocks, bonds, bullion, bills of exchange, or promissory notes for purchase or sale other than on commission, shall be regarded as a private banker within the meaning of the Clayton Act, but this definition shall not include firms or individuals who do a business only of buying and selling stocks, bonds, or other securities on commission, or who receive funds only for the purpose of buying and selling such securities as the agent or broker for others."

Respectfully,

M. C. ELLIOTT.
Counsel.

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

9/21/16

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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

811

September 22, 1916.

Dear Sir:

In reply to several inquiries, the Board suggests that the Federal Reserve Banks adopt a new ledger item entitled "Member banks' collateral notes" to include advances for a period not exceeding 15 days on promissory notes of member banks secured by eligible collateral (in accordance with recent amendment of Section 13 of the Federal Reserve Act) and report daily in the first subdivision of Form 34 holdings of this paper (Code word "BANK"), also include the respective amounts in the totals shown in the daily "Sac" telegrams.

It is suggested that collateral loans to member banks be reported on separate sheets of Form BD-4, under caption "Member banks' collateral notes", that the items of this class be numbered separately and that instead of a schedule of items deposited as collateral the total of daily transactions on Form BD-4 under this head be followed by a statement bearing the signature of an officer of the bank certifying that items numbered - - - - represent loans to member banks on their promissory notes fully secured by eligible paper (or by the deposit or pledge of bonds or notes of the United States) in accordance with amended Section 13 of the Federal Reserve Act.

It is further suggested that the banks report at the end of each month on Form 40 the amounts of collateral loans granted to member banks in each State under captions "10 days and less", "over 10 to 30 days", and "Total". A suitable supply of revised Form 40 will be sent to your bank within a few days.

Very truly yours,

Governor.

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AND FISCAL AGENT

ADDRESS REPLY TO
812 FEDERAL RESERVE BOARD

September 22, 1916.

Dear Governor:

Referring to the matter of supplements to the par list you are informed that this matter has had the consideration of the Board and it has been determined to send the next supplement to the par list to member banks of the system with the Federal Reserve Bulletin. It will, therefore, go out about the first of November. It is thought that this will simplify the matter for Federal reserve banks since it relieves them of sending the supplement to the par list to member banks. Federal reserve banks will, however, under this arrangement, continue to send the par list to banks not members of the system. Will you please advise of the number of copies you will require under this new arrangement?

It will be necessary for mail advice of changes in the par list to reach Washington on October 20th. Changes can, however, be made by telegraph to and including October 25th and as received will be incorporated in the proof.

Very truly yours,

Governor.

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RESOLUTION ADOPTED BY THE FEDERAL RESERVE BOARD

September 22, 1916.

oOo

WHEREAS, It appears that the twelve Federal reserve banks have purchased in the open market bonds in excess of the amount which might have been allotted to such banks at the end of this quarterly period on the basis heretofore determined upon and announced by the Board.

NOW, THEREFORE, BE IT RESOLVED, That it is the sense of the Board that no necessity exists for enforcing the requirement provided for under Section 18 of the Federal Reserve Act at the end of this quarterly period ending October 1, 1916, and that it will not at this time require the Federal reserve banks to purchase any of those bonds which are offered for sale by member banks through the Treasurer of the United States under the provisions of Section 18.

BE IT FURTHER RESOLVED, That the Secretary be instructed to send a copy of this resolution to the various Federal reserve banks and to the member banks which have offered bonds for sale in order that they may be notified of the action of the Board in the premises.

9/22/16

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

817

September 27, 1916.

Dear Sir:

Referring to previous correspondence, particularly letter of September 9 regarding statistics of cost of your clearing department, the Board requests that in your September and subsequent statements of earnings and expenses (Forms 286-b and 287-b) you show the expenses of your bank gross, i. e., including all expense a/c transit department. It is also suggested that the latter expense, segregated by items, be shown on a separate sheet of Form 287-b, while the amount of service charges be reported as a memorandum item on a separate sheet of Form 286-b, which should also give the itemized cost of furniture and equipment charged to the transit department.

On your statement of gross current expenses (Form 287-b) please report as a deduction below item HALL the aggregate expense of your transit department, and show as a difference the net current expense of the bank proper.

In order that the Board may have comparable figures for all banks, it is requested that the September figures of the cost of furniture and equipment (Items GLEN to HOLT), as well as the cumulative figures of current expenses for the 9-month period, be adjusted, wherever necessary, so as to show the combined cost and expense inclusive of the respective amounts charged to the transit department.

Very truly yours,

Assistant Secretary.

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AND FISCAL AGENT
818
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

Federal Reserve Bank,

Sirs:

You will find inclosed herewith a transcript of your account with the Federal Reserve Bank of as shown by their books at the close of business Please compare with your records and return the inclosed reconcilement to the undersigned in care of Federal Reserve Board, Washington, D. C.

It will also be appreciated if you will inclose with the reconcilement a transcript of your ledger account, giving in detail all entries made five days prior and eight days subsequent to the day of examination.

You are also requested to inclose a transcript of the account of that bank with your institution, giving in detail all debits and credits entering into the account for the period from to Please describe each entry separately, giving the date of the remittance letter and the source from which received.

Respectfully,

Federal Reserve Examiner.

Inclosures.

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SHERMAN ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

819

September 27, 1916.

Dear Sir:

Question has been raised as to whether the recent amendment to the Federal Reserve Act reading in part as follows:

> "Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice and protest by such bank as to its own endorsement exclusively, any Federal reserve bank may discount notes, drafts, and bills of exchange arising out of actual commercial transactions;* *"

means that hereafter nothing will be required of member banks in the way of indorsement upon paper offered for discount except their simple written indorsement.

You are advised, for your information and the information of any member banks which may be in doubt as to the procedure, that such simple written indorsement will be regarded as satisfactory and as coming within the terms of the law.

Respectfully,

Assistant Secretary.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

822

October 2, 1916.

Dear Sir:

At the recent conference in Boston each of the Governors present gave approximate figures of the cost of clearing and the opinion was freely expressed that the figures fixed by the Transit Committee of 1½¢ per item was more than high enough to fully cover the actual cost, omitting it is true, certain overhead expenses, which it was thought should not be charged to this account.

The belief was also generally expressed that it was desirable to keep the cost down to the point where the Banks would be rendering this service to their members on a cost basis and not on a basis that would yield them profit.

More recent experience indicates a cost in Boston of 9/10ths of a cent, and in New York of 1 cent per item, so that the time seems not far distant when this important service can be rendered to member banks not for 1½¢ per item but for perhaps one half that cost, and eventually as an expense which can be absorbed as part of the operating expenses of the Reserve Banks. This would tend greatly to popularize the service, and perhaps go farther than any one thing to bring in State Banks, hence we should be glad to know what you think can be done in the matter.

Very truly yours,

Chairman, Committee on Clearing.

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY

ADDRESS REPLY TO
FEDERAL RESERVE BOARD
821

October 2, 1916.

Dear Sir:

In answer to several inquiries as to the proper treatment of profit realized on sales of United States bonds, it is suggested that such profit be entered on the books and reported on Form 34 as an earning under the heading "Sundry profits", such items to be transferred, together with other earnings, to the Profit and Loss account at the periodical closing of the books. In this connection it is further suggested that no entries be made on the Profit and Loss account except at the time that the books are closed.

On the monthly statement of Earnings, Form 286 B, the total profits realized on the sales of United States securities should be reported under the separate head "Profit on United States Securities Sold".

Inasmuch as a number of the Reserve Banks have already transferred discount on United States bonds to the Earnings account, no objection will be made by the Board to a similar transfer being made by the other Federal Reserve Banks.

Very truly yours,

Secretary.

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CHARLES S. HAMLIN
825.

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

October 2, 1916.

My dear Governor:

This office has been asked for an opinion on the question of whether or not a bank located in the outskirts of Chicago, but within the city limits, may make loans on real estate under authority of Section 24 of the Federal Reserve Act.

Section 24 provides in part 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".

This language is free from ambiguity and while it may work a hardship on the small banks in the outlying districts of central reserve cities, the Board is without power to grant them immunity.

As Chicago is a central reserve city a bank located within its limits is not authorized by the terms of the Act to make real estate loans.

Respectfully,

M. C. ELLIOTT,

Counsel.

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

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AND FISCAL AGENT

ADDRESS REPLY TO
828 FEDERAL RESERVE BOARD

I inclose herewith for your information copy of a letter received from Mr. E. N. Hurley, Chairman of the Federal Trade Commission, under date of September 18th. Mr. Hurley addressed me in this communication because of our past acquaintance and for the further fact that we have discussed the general bearing of this particular problem on the work of the Federal Reserve Board as well as of the Federal Trade Commission. While Mr. Hurley has impressed me very much with the importance of the subject, I have an open mind on the question, and would like, before presenting it to my colleagues on the Federal Reserve Board, to have the opinion of prominent bankers upon it. May I ask you, therefore, to kindly take Mr. Hurley's proposal under consideration and give me your views as to the feasibility of carrying it out?

Yours very truly,

Member, Federal Reserve Board.

Inclosure.

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828-a

FEDERAL TRADE COMMISSION

WASHINGTON

September 18, 1916.

Hon. Frederic A. Delano,
Federal Reserve Board,
Washington, D. C.

My dear Mr. Delano:

In view of our many conversations on business conditions as found by the Federal Trade Commission, I wish to call to your attention the deplorable lack of adequate accounting methods in our industries. In order to remedy this condition, the Federal Trade Commission has been doing educational work along accounting lines. This work has been very effective. We are sending out daily to manufacturers and merchants upon request about 2,000 of our accounting pamphlets. We have received thousands of letters approving our work and showing the necessity for further effort in this direction.

In the second place, the Commission is cooperating with many trade associations which are endeavoring to get their members to adopt sound accounting systems. We send our experts to meet with them and discuss the features of cost accounting that are peculiar to the particular industry. We tell them to work out a system of cost keeping. When they bring it in the Commission will counsel with them and will approve it as a basic system for that industry. With this general standard officially approved, details to vary, of course, with the individual companies, the association has a strong argument to bring its members into line with sound accounting.

Much more should be done, however, to insure the preparation of financial statements which will show the true standing of business concerns.

In our investigation we have found a very decided tendency on the part of business men to overvalue their assets and

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frequently to understate their liabilities. The overvaluation of assets is, in a large measure, due to the failure of business men to make adequate provision for depreciation. In many cases, the difference between the value of the assets shown by financial statements and the actual value is so great that many concerns showing a comfortable surplus are in fact insolvent. It is also important in this connection to consider how much of expenditures for jigs, tools, dies, and patterns are properly chargeable to capital, and how much to the cost of production.

In many cases of commercial failure concerns had made statements for credit purposes, a comparatively short time before their failure, which showed them to be in good financial condition. This is true even in some cases where statements have been prepared by public accountants.

The great difficulty is that no matter who prepares the statement, whether the manufacturer or merchant himself, or a public accountant, the person preparing it is either the prospective borrower or some one in his employ, and the natural tendency is to make as favorable a showing as possible.

In order to increase the reliability of balance sheet statements and to enable the banker to place more confidence in them, some plan must be devised whereby the authority of the banker over the accountant will at least equal that of the borrower, particularly as to the form of the statement and as to the methods used in determining the value of assets and the ascertainment of liabilities.

Knowing your interest in this matter, I now wish to suggest a plan which I am sure will accomplish this result and place our industries on a much sounder basis. The plan suggested is, first, that a standard form of statement be prepared, on which form all statements for credit purposes be made. Second, a general set of rules be laid down for the valuation of assets and the ascertainment of liabilities, and these rules subscribed to by the accountant and followed by him in the preparation of statements. Third, all statements be prepared or verified by an accountant who has registered with the Federal Reserve Board or the Federal Reserve Banks, and the Board or Banks should have the authority to revoke the registry of an accountant for any unreliable work, after giving

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the accountant an opportunity to be heard. This plan, if followed, we believe could not help but result in the presentation of more complete and accurate statements. The rules could be drawn by the American Association of Public Accountants for the approval of the Federal Reserve Board or Banks.

It is well known that public accountants are willing and ready to do their part in having the banker presented with a balance sheet that will show a concern's true financial position. The trouble is that many business men disagree with the public accountants as to what shall be written off for depreciation, and how other items shall be treated. The accountant, although desirous of being conservative, realizes that unless he agrees with his client he is likely to lose him. The result is usually a compromise.

Bankers and public accountants have a vital interest in every movement that makes for the welfare of American business and general prosperity. It is to their interest, and it is a part of their responsibility, to do their share towards bringing about a better knowledge of business conditions. and greater efficiency.

I firmly believe that a close cooperation as outlined above is bound to be directly helpful to every manufacturer and merchant in the country.

I appreciate that present bad methods can not be remedied in a short time, but a start must be made in some cooperative way. If the Federal Reserve Board, the bankers of the country, and the American Association of Public Accountants will work with the Federal Trade Commission in its labors with the various trade associations of manufacturers and merchants, I am sure a great deal can be accomplished within a comparatively short time.

I hope the Federal Reserve Board will find it possible to give this matter special attention. The Federal Trade Commission will be pleased to furnish detailed information to substantiate its views.

With kind regards, I am

Very truly yours,

EDWARD N. HURLEY
Chairman.

10/6/16

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....ANNOUNCEMENT BY THE BOARD....

Section 8 of the Clayton Act, which becomes effective on October 15, 1916, prohibits private bankers under certain conditions from serving as officers or directors of member banks.

A number of inquiries have been received asking the Board's interpretation of the language "private banker" as used in the Clayton Act. As the Board is required, under the provisions of the Clayton Act, to prosecute those violating its terms, it is necessary that it should make clear its interpretation of the language used in order that the banks may comply with the letter and spirit of the Act.

The purpose of the Act, as its title implies, was to prevent unlawful restraints and monopolies. It is obvious, therfore, that Congress intended to prohibit common control of member banks and of private bankers engaged in the same activities as member banks, and that it intended to preserve competition in cities of more than two hundred thousand inhabitants between member banks, private bankers, and other incorporated banks, and likewise intended to preserve competition between member banks, regardless of their location, and State banks, trust companies, or private bankers having aggregate resources of more than five million dollars.

In this view the Board interprets the term "private banker" to include partnerships or individuals who are engaged in the banking business, as that term is generally understood, -- including those partnerships and individuals who solicit or receive deposits subject to check, who do a foreign exchange, acceptance, loan or discount business, or who purchase and sell and distribute issues of securities by which capital is furnished for business or public enterprises.

The term "private banker" is interpreted not to include the ordinary stock, note, or commodity broker, unless a substantial proportion of his profits are derived from, or a substantial part of his business consists in, one or more of the banking activities described, nor is it interpreted to include partnerships or individuals using only their own funds in making loans or investments.

No private banker whose partnership or firm assets aggregate more than five million dollars is eligible, under the terms of the Clayton Act, to serve as a director of any member bank, and no private banker, regardless of the amount of partnership or firm assets, is eligible to serve as a director, other officer or employee of any member bank located in a city of more than 200,000 inhabitants, if such firm or partnership is located in the same city.

The Kern Amendment to the Clayton Act does not authorize the Federal Reserve Board to grant permission to such private bankers to serve as officers or directors of a member bank even though it appears that they are not in substantial competition with such member bank.

October 6, 1916.

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1501

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AND FISCAL AGENT

832 ADDRESS REPLY TO
FEDERAL RESERVE BOARD

S I R :

I enclose herewith copy of an announcement (no. 930) issued by the Federal Reserve Board in reference to the definition term "private banker" as employed in the Clayton Act as amended. This definition supersedes the opinion of Counsel, dated September 9th (no. 809) and sent to you on September 15th, last.

Very truly yours,

Secretary.

Mr.
Chairman, Board of Directors,
Federal Reserve Bank of

Enclosure.

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AND FISCAL AGENT

833

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

Apparently superseded by 833a

Dear Sir:

This will remind you that copy covering business conditions for the Federal Reserve Bulletin, to be issued on the first of next month, will be welcome in the office of the Federal Reserve Board not later than the 23rd of this month. Its prompt receipt will aid in getting the Bulletin out on time.

In sending this copy will you also include data similar to that found on page 511 of the Federal Reserve Bulletin for October, from which a statement can be prepared as to the operation of the clearing plan.

There have been sent you slips on which the Board requests that you fill in briefly answers to the questions covering conditions in general business, crops, bank clearings, and other indications of general trend. Please return one of these slips with each report of business conditions. They are desired for the purpose of making an accurate summary of conditions in the United States.

Very truly yours,

Secretary.

P. S.

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1503

EX-OFFICIO MEMBERS

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 11, 1916.

Dear Sir:

This will remind you that copy covering business conditions for the Federal Reserve Bulletin, to be issued on the first of next month, will be welcome in the office of the Federal Reserve Board not later than the 22nd of this month. Its prompt receipt will aid in getting the Bulletin out on time.

In sending this copy will you also include data similar to that found on page 598 of the Federal Reserve Bulletin for November, from which a statement can be prepared as to the operation of the clearing plan.

There have been sent you slips on which the Board requests that you fill in briefly answers to the questions covering conditions in general business, crops, bank clearings, and other indications of general trend. Please return one of these slips with each report of business conditions. They are desired for the purpose of making an accurate summary of conditions in the United States.

Changes in the par list should reach Washington on November 22nd.

Very truly yours,

Secretary.

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Released for the afternoon of October 12:

Mr. Willis said:

"The Philippine National Bank, provided last winter by Act No. 2612 of the Insular Legislature, has been successfully established, and at the time of my departure from the Islands on August 31, was in excellent condition, and had every reason to expect a successful future. The Bank has been assigned an authorized capital of 20,000,000 pesos, or $10,000,000 in American currency. Of this amount 10,100,000 pesos, or $5,050,000, has been subscribed by the Government, and the money to take up the stock appropriated. The Government subscriptions are payable in instalments, however, and in the meantime the balance of the stock has been placed on the market and offered to private subscribers. Sales of the stock were steadily being made in lots of varying size, and there is every reason to suppose that the privately owned shares will be widely distributed throughout the Islands by the time the Government subscriptions are fully paid up. The Philippine National Bank is the depositary of the Insular Government, of all municipal governments including the city of Manila, of the provincial governments, of the postal savings bank, and of various other institutions. It is expected that when the transfer of the Manila and Dagupan Railway to the Insular Government has taken place, the financial operations of the railroad will be entrusted to the Philippine National Bank.

The Bank thus has a large volume of purely Governmental business to transact. If has not, however, confined itself to Governmental operations, but has also begun the receiving of general deposits, and has been the recipient of funds from a large number of private depositors, many of them business men in Manila, or other cities of the Philippines. Foreign exchange business has been undertaken by the Bank on a substantial scale, and relations have been established with the principal places on the China coast and in Japan, while good banking connections have been effected in New York, London, and other American and European cities. The Bank is advertising that it intends to make a specialty of

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foreign transactions designed to facilitate the exportation and importation of Philippine products, and has already succeeded in attracting to itself a good deal of business of this description.

The prosperity of this, as well as of other banks of the Philippines, of course depends upon the general business situation in the Islands. There seems to be no reason to doubt the soundness of that situation. Exports and import business is steadily advancing and prices of nearly all products were very high at the time I left the Islands. The greatest obstacle to the full development of business is found in the transportation situation, which, of course, has been bad all through the European war, and has been particularly trying during the last few months owing to the obstacles placed in the way of the transaction of business and of the movement of goods as the result of the action of the various belligerent countries. In spite of this handicap, trade is generally admitted to be in a very promising and satisfactory state. The sugar industry, with things as they are in the world's sugar market, is highly profitable wherever modern machinery has been installed as it has at a number of points in the Islands. Very substantial interest in the sugar situation is being shown by outside investors, and there is abundant reason to expect that in the near future there will be a large development of modern sugar mills equipped with proper machinery and able to produce good centrifugal sugar for export. The cocoanut oil industry is also showing marked development, the business of extracting the oil on the spot having been recently introduced in place of the older method of shipping the copra abroad for the extraction of the oil. The cigar business has been greatly stimulated by the high prices of tobacco in Europe and the United States. Hemp is high in price and as usual is in strong demand. In consequence of the good prices realized for their products the natives have become better customers than in the past, and their desire for American goods of all kinds makes the Islands a desirable market for textiles, automobiles, iron and steel products of all kinds, various forms of wearing apparel, particularly shoes, canned goods, and a great variety of manufactures, particularly those which have a relatively large value in small bulk, and hence are able to bear comparatively high rates of freight.

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One serious obstacle to the growth of business in the Philippines has been the lack of capital and the high rates charged for loans both at banks and elsewhere. The new Bank may be able to relieve this condition in some measure, and is endeavoring to do what it can in that direction, but real relief will come only from the larger investment of funds in the Islands by American capitalists. While it may be a good while before general investors in the United States become very deeply interested in Philippine opportunities, those who are familiar with the business openings in special lines, such as those I have referred to above, are already manifesting genuine interest and in a practical way. The Philippines are developing their trade not only with the United States but also to a very considerable extent with Japan, and in a somewhat lesser degree, with China. Chinese trade has been badly crippled by the revolutionary activities that have been in progress in that country, but conditions appear to be steadily growing more stable there, and as they do, the trade of the Philippines with China will improve still further. Due to the absorption of English merchants in conditions growing out of the war, and to the present forced withdrawal of German money from the field, there is now an unusual opening for American capitalists in China. As recent announcements have shown this opening is being availed of on a very large scale by some of the more enterprising, and there are many indications that small operators will shortly begin to further the sale of American goods in China, recognizing that a very unusual opportunity is now presented to them. Up to date much of the advantage thus offered has been absorbed by the Japanese, but it is likely that they will not long be allowed to enjoy these new and exceptional advantages without competition. While the Philippines can obtain an important and valuable share in this new Chinese trade, the opportunity is one that is a good deal more valuable to American business men than to those in the Philippines. The Philippines for a long time to come will be largely a market for American manufactures, just as China will be, and the trade of the Islands with China will consist largely in the exchange of raw products. The organization of the new bank is intended to assist all these trade movements, and so far as possible to encourage the investment of capital from the United States in the Islands, with the assurance of stable and reasonable accommodation to all forms of legitimate business."

10/10/16

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STATEMENT FOR THE PRESS.

October 13, 1916,

The Federal Reserve Board today, acting upon the appeal of certain Wisconsin bankers, voted to transfer the territory included in the counties of Monroe, Jackson, Clark, Marathon, Langlade, Oconto and Marinette, of Wisconsin, and all other counties in the same State now in the Minneapolis District east and south thereof, from the Minneapolis to the Chicago District. No change as to northern Michigan.

The transfer was made effective as of January 1, 1917.

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FEDERAL RESERVE BOARD

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ADOLPH C. MILLER
CHARLES S. HAMLIN

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

843

October 17, 1916.

Dear Sir:

Our Statistical Division is about to revise Form 34, Daily Bank Statement, preparatory to ordering the new supply for the coming year. May I ask you to have your experts look over carefully the form used at present and to state in what particulars it may be changed to meet the new requirements and changed conditions of your bank. Any suggestions along these lines will be gratefully received and given proper consideration.

Hoping to hear from you in this matter at an early date, I am

Very truly yours,

Secretary.

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UNITED STATES BUREAU OF EFFICIENCY
WASHINGTON

August 26, 1916.

The Governor,
The Federal Reserve Board.

Sir:

On May 16, 1916, the Senate adopted a resolution providing as follows:

> That the Bureau of Efficiency is directed to prepare and submit to the Senate estimates of the immediate and ultimate cost of pensioning or retiring the civil employees of the United States, and in order to prepare such estimates, the Bureau of Efficiency shall obtain from the Executive Departments, from the Chiefs of Bureaus and independent establishments, such information regarding persons appointed to and separated from the Executive Civil Service as may be necessary for that purpose, including their salaries and dates of birth, appointment, and separation;
>
> That for said purposes, the heads of the Executive Departments, Chiefs of Bureaus and other executive or administrative officers, are hereby directed to furnish the said Bureau of Efficiency with said information.

On investigation it was found that the information needed to comply with the foregoing resolution is also needed for two other purposes -- (1) to enable the Census Bureau to publish a statistical bulletin on the Executive Civil Service similar to that published in 1907 and (2) to expand the partial roster of civil employees that is now maintained in the Civil Service Commission. It is hoped that if this roster can be made to show all the information regarding civil employees that is needed for the biennial register of the United States and for statistical purposes, it may be possible to avoid calling on the Departments for any further reports of this kind regarding their employees except current reports of changes.

Under the circumstances, it has seemed desirable to utilize the inquiry authorized by Senate Resolution of May 16, 1916, for the other two purposes mentioned above. This Bureau has therefore cooperated with the Census Bureau and the Civil Service Commission in preparing a card schedule calling for all information needed by the three offices. Samples of this schedule are enclosed herewith, with the request that they be filled out and returned to the Bureau of Efficiency as promptly as possible, in order that the extensive tabulations and computations necessary to estimate the cost of retirement plans may be completed before the opening of the next session of Congress.

If all the information called for on the schedule is not of record in the Department, it will be necessary to obtain it from the employees before filling in the schedules. The following form showing the inquiries that it is necessary to make of the employees in one Department is submitted as a suggestion.

* * * * *

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In order to facilitate the work of tabulation, the cards should not be held until all are finished, but should be sent in from time to time as completed. Cards for different bureaus, offices, and services should be wrapped separately, and each package should be marked on the outside with (1) the name of the bureau, office or service, (2) the number of cards sent, and (3) if possible, the approximate number still to come.

With the final lot of cards for each bureau, office, or service, a statement should be transmitted on Form No. 10 (sample herewith) showing the total number of employees reported and their total annual rate of pay.

In order to enable the Bureau of Efficiency to determine the rate of separation from the public service (which is necessary in order to estimate the cost of a retirement or pension plan) it is also requested that a report be made of the separations from each bureau, office, and service during the five years ended June 30, 1916. A sample copy of a schedule for use in making these reports is enclosed herewith.

It is suggested that you designate an employee to represent your Department in conference with this Bureau and other offices concerned and that you instruct him to submit for discussion, as promptly as possible, a list of the classes of employees that it is planned to include and exclude under the instructions on the schedules.

A supply of the schedules and other forms will be forwarded in a few days. Should additional copies be needed they will be furnished promptly on request to the Bureau of Efficiency.

Respectfully,

HERBERT D. BROWN.

Chief, Bureau of Efficiency.

10/18/16

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At a stated meeting of the Federal Reserve Board, duly held at its office in the City of Washington, District of Columbia, October 12, 1916.

P R E S E N T :

Mr. Harding, Governor,
Mr. Warburg, Vice Governor,
Mr. Hamlin,
Mr. Delano,
Mr. Miller,
Mr. Williams.

In the Matter of Readjusting the Geographical Limits of Districts Nos. 7 and 9 in accordance with the power vested in the Federal Reserve Board by Section 2 of the Federal Reserve Act.	ORDER AMENDING THE GEOGRAPHICAL LIMITS OF DISTRICTS NOS. 7 AND 9.

WHEREAS, the Federal Reserve Board is authorized and empowered by Section 2 of the Federal Reserve Act to readjust the Federal reserve districts; and

WHEREAS, upon further consideration of -

(a) The petition of certain banks in Wisconsin for the transfer from district No. 9 to District No. 7 of all that part of Wisconsin situated in District No. 9 east of the western boundaries of the counties of Ashland, Price, Taylor, Clark, Jackson and Monroe;

(b) The answer of the Federal Reserve Bank of Minneapolis;

(c) The briefs of counsel and arguments heard by the Federal Reserve Board;

it appears to such Board that the convenience and customary course of business and the best interests of the Federal Reserve System will be served by a readjustment of the geographical limits of districts Nos. 7 and 9;

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NOW, THEREFORE, the Federal Reserve Board doth order -

(1) That district No. 7 be readjusted and altered so as to include the State of Iowa, all that part of Wisconsin located south of the northern boundary of the counties of Marinette, Oconto, Langlade, Marathon, and Clark; and east of the western boundary of the counties of Clark, Jackson, Monroe, Vernon, Crawford, and Grant; all of the southern peninsula of Michigan, viz, that part east of Lake Michigan; all that part of Illinois located north of a line forming the southern boundary of the following counties: Hancock, Schuyler, Cass, Sangamon, Christian, Shelby, Cumberland, and Clark; and all that part of Indiana north of a line forming the southern boundary of the following counties: Vigo, Clay, Owen, Monroe, Brown, Bartholomew, Jennings, Ripley, and Ohio;

(2) That district No. 9 be readjusted and altered so as to include the States of Montana, North Dakota, South Dakota, Minnesota, all that part of Wisconsin not included in district No. 7, and all that part of Michigan not included in district No. 7;

(3) That the alterations in districts Nos. 7 and 9 directed in this order become effective January 1, 1917;

(4) That the Federal Reserve Banks of Chicago and Minneapolis be notified of the changes made in the districts referred to and directed to take such action as may be necessary for the transfer of membership of the banks included in the territory affected;

(5) That a copy of this order be filed with the Comptroller of the Currency in order that the certificate of the Reserve Bank Organization Committee may be properly amended.

W. P. G. HARDING,

Governor.

Attest:

H. PARKER WILLIS,

Secretary.

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FEDERAL RESERVE BOARD

WASHINGTON.

October 19, 1916.

Mr. J. Z. Miller, jr.,
Governor, Federal Reserve Bank,
Kansas City, Mo.

My dear Mr. Miller:

Referring to your letter of October 14th about assessing penalties for deficient reserve balances, I realize the difficulties that you are laboring under and our Board would not be unwilling to get out some general order on this matter. The fact of the matter is that some of the banks have already issued penalty notices and are collecting penalties. The Board has taken the position that there is no objection to waiving the penalties for the months of July, August and September, or for such a period, within reason, as the Federal Reserve Bank of the District may recommend as being desirable, for the reason that the clearing system was in a more or less formative condition. Now, however, it seems to me that the time has come when the assessment of penalties for deficiencies in reserve should be made and, while it is proper that banks should have fair notice of this, I see no reason why it should not be made effective, say November 1st.

I have discussed with some of the Federal Reserve Banks the desirability of assessing this penalty not on the basis of a daily statement of reserves, but on the basis of a weekly average. Everyone with whom I have talked seems to admit that there are some objections to the average basis, and this is especially true when it comes to the monthly average, but on the other hand, the difficulty in making the assessment on the daily basis is so great that an average of at least a week's business should be taken. The experience in some districts of assessing penalties has been to make the member banks pretty careful and vigilant in keeping up their reserves, and I think you will find this to be the case. The important thing to remember is that we do not want to make

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revenue out of penalties; what we want to do is to compel banks to maintain their reserves, as the law requires.

If you want the backing of the Board in this matter, I suggest that you send us the form of circular which you propose to issue and we will give it our approval, if we approve it, or if we have some suggestions to make we will approve it as amended.

Yours very truly,

(Signed) F. A. DELANO,

Enclosure

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EX-OFFICIO MEMBERS
WILLIAM G. McADOC
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

October 19, 1916.

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

My dear Mr. McCord:

On behalf of the Committee of the Federal Reserve Board on Clearing I inclose herewith copy of a letter which has been received from Mr. George P. Thompson, President of the Wholesale Grocers' Association of New Orleans. The Board has not answered this letter, but our disposition would be to tell Mr. Thompson that he must not expect too much all at once. We find that a good many clearing house associations are disposed to get the full benefit from the service rendered by Federal Reserve Banks in the form of low service cost, yet undisposed to revise their rules so as to pass any of this advantage on to the ultimate consumer.

Under the law it is the duty of the Board to fix a schedule of charges which banks may assess against their patrons, but the Board has felt that this was an authority it did not care to exercise, at least until the new clearing system was working smoothly and banks and bankers had had a full opportunity to revise their charges. Furthermore, we would a great deal rather let the clearing house associations fix charges which might be submitted to us for approval. If, however, we find the disposition on the part of clearing house associations not to take up this matter in the right spirit, the Board will have no other option than to establish a schedule of charges. I am reasonably confident that the matter can be adjusted by you through a conference with the New Orleans bankers, and I will, therefore, ask that you take the matter up and inform me how you succeed.

Yours very truly,

(Signed) F. A. DELANO.

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EX-OFFICIO MEMBERS

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SECRETARY OF THE TREASURY
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COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

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October 19, 1916.

Dear Sir:

I am sending you herewith copy of a letter to Governor McCord in reference to a complaint made against the rules of the New Orleans Clearing House. As you are doubtless aware quite a number of clearing house associations have neglected to modify their rules in any way since the new clearing system went into effect, and it may become necessary for the Federal Reserve Board to act. However, it is desirable that each association should voluntarily readjust its own rules rather than to have any compulsion on the part of the Board; hence we would be glad if you would discreetly suggest such action.

In this connection I should be glad to know what progress is being made in your District in the adjustment of this matter.

Yours very truly,

Chairman, Committee on Clearing.

Inclosure.

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WHOLESALE GROCERS' ASSOCIATION OF NEW ORLEANS

NEW ORLEANS

October 10, 1916.

FEDERAL RESERVE BOARD
Washington, D. C.

Dear Sirs:

I have, in behalf of this organization, been agitating the collection of country checks at par. I have taken up the matter with the local clearing house and they have promised to appoint a committee to revise the present rates, but what we are after is "Country Checks at Par" as is intended by the Reserve Board. We note from the local press of October 5th that Mr. J. W. Bolton, of Alexandria, Louisiana, president of the Louisiana Bankers Association, says "No honest efforts will be spared for the country bankers but the pressure behind the bills before Congress which are intended to thwart the Federal Reserve Board plan for a universal collection of country checks without exchange charge." We have followed this subject in the press and otherwise and are very much impressed with the work that has been done so far. If you can give us any data as to the increased usefulness of this new plan, we would appreciate same. Matter that would help us with the local clearing house. We find a good many banks in this immediate vicinity, country banks that are clearing checks at par so advertised in the paper or otherwise notifying the trade, but our local institutions in New Orleans have not met this issue in the same spirit as we thought they should, and we believe that if you could give us something that we could work along to encourage them in correcting conditions. We would appreciate it very much. As we see it the establishment of this new measure should take place without further delay in order to prevent any attempt to influence Congress later on during the coming session to do something antagonistic to the clearing of country checks at par.

Yours very truly,

(Signed) GEORGE P. THOMPSON
President.

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Released for publication

when delivered but not earlier than

12.00 o'clock noon, Oct. 24, 1916.

---oOo---

THE FEDERAL RESERVE SYSTEM: LOOKING AHEAD

(Managing the gold supply to meet a foreign drain)

Address

of

A. C. M I L L E R

Member of the Federal Reserve Board.

---oOo---

Delivered Oct. 24, 1916
at the Annual Convention of the

INDIANA BANKERS' ASSOCIATION

at Indianapolis

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THE FEDERAL RESERVE SYSTEM: LOOKING AHEAD.
(Managing the gold supply to meet a foreign drain)

"The European war has pushed forward the day on which America has taken its place as a leader in the international money market, and its banking system had, in the very nick of time, been reorganized in such a way that it is ready to face the problems of international finance..... The new system came into being at a time of stress, and so far has faced with admirable composure and success a series of problems for which no experience could have prepared it. America is now one of the leading powers in international finance, and on the wise and skillful use of its strength the future prosperity of the civilized world will, to a great extent, depend." These words, quoted from a recent book on international finance by Hartley Withers, England's most brilliant financial writer, reflect the growing appreciation of the profound alteration which has taken place in the position of our country in the sphere of international finance resulting from the disorganization and dislocation in established relationships and ways of doing things growing out of the great war. Mr. Withers has not exaggerated the change in our situation and the new responsibilities with which our country is being confronted in the region of world finance.

The world has changed much during the two years since the Federal Reserve System was put into operation, and there is every evidence that it is going to keep on changing at a rapid pace and for a long time to come. We are right now in the midst of a most acutely

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transitional position - more marked than any that has ever hitherto overtaken our foreign commerce. Our commerce is changing and will keep on changing, not only in its magnitude but in its character; we shall be trading in new things and with new countries and our industries are changing to keep pace with our commerce. And since the country's obligations and opportunities in the field of international finance depend upon its position in international commerce, it is clear that our banking machinery must change and gain in strength to accommodate our expanding and changing commerce. In the last two years, we have lived through a generation. Changes in our banking methods and the scope of banking operations which were foreshadowed in the Federal Reserve Act, and for which provision was then made for the first time in the history of American banking legislation, are coming with a speed which was not anticipated and which could not have been anticipated. Before the outbreak of the European war, our country had very little to do in the field of international finance except as a borrower and so it had no occasion to develop the machinery of international banking. It sought such international banking facilities as it required from other countries, and took them on such terms as were given. American banking had been developed strictly on domestic lines as an incident to the internal development of the country's industry and trade. The country was so large and rich, and offered so attractive a field for the investment of capital at home, that it left little or no margin of surplus banking capital for foreign operations, but instead attracted immense investments of foreign capital to it. As long as this condition continued we were content to let other countries take

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care of the business of international banking so far as our needs were concerned, for much the same reason that we were content to let other countries supply our needs for ocean carrying service.

More than one occasion, however, had shown that the time was approaching when our country must look to its own facilities and resources for a larger measure of accommodation in international banking. The dependence upon foreign countries was being felt to be precarious. The Federal Reserve Act, therefore, undertook to create agencies which would give to the banking machinery of the country a greater measure of control over those factors in international finance which were of consequence to the stability and ease of American trade. For this purpose, it authorized National banks to establish foreign branches; for the first time it authorized National banks to accept against transactions arising out of the foreign trade of this country; in brief, created "dollar exchange". And what is perhaps destined to be of equal importance with either of these, it authorized the Federal Reserve Banks with their considerable resources to enter the field of foreign banking by the establishment of foreign agencies and correspondents in any part of the world, and to engage in operations in foreign exchange, purchase and sale of bullion, etc. How much the unprecedented prosperity that our foreign trade and industry have enjoyed during the past two years is due to the banking facilities created by the Federal Reserve Act, it would be difficult to exaggerate. The acceptance business, hitherto a strange and unknown field in American banking, has been entered with marked success; "dollar exchange", hitherto an unknown quantity or symbol in the world of international commerce, is

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now recommending itself to the favor of trading nations as the most stable unit of international payment. To maintain our exchange on a stable basis through lean times as well as through fat times, is clearly so important a prerequisite to our expanding commerce and industry as to make the agencies of its maintenance and control a matter of primary concern to every banker and business man in the nation. The never-to-be-forgotten events of the early autumn of 1914, when there was a complete demoralization of the foreign exchanges and a more or less complete suspension of trade, need only to be recalled to induce an appreciation of what stable exchange means to a country. The heroic and costly efforts which England and other foreign countries have been making to protect their trade with the United States by stabilizing their exchange as far as they could through shipments of gold, shipments and sales of securities, and borrowing, emphasize the same truth, and suggest that we should carefully examine our banking machinery with a view to determining whether it is in all respects equal to the task of doing the work in international finance which is clearly destined to fall to us in the critical period of reconstruction which will be entered upon by the great trading nations after the conclusion of the war.

For we shall have to do our part, not only industrially and commercially but also financially, in helping the nations and peoples of Europe to industrial and financial rehabilitation when this most costly and destructive of wars is finally finished. Banking responsibility always attaches to countries which are financially strong and able. The American banker is clearly destined to have not only a place of larger importance in the affairs of his own country, but to play a role

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of first importance in the affairs of other countries. Now is the time to get ready for this work, so far as we are not yet fully prepared; to take reckoning of the demands which will be made upon us; to take stock of our resources and capabilities, and to supplement these where they seem inadequate.

There are many different angles to the problems of international finance which may be expected to affect us after the war. There is one in particular, however, which has riveted the attention of banking circles of late and been regarded by many as of such vital concern as to make it a problem of great urgency. It is the problem of devising effective ways of dealing with our gold supply. It is this problem to which I venture to direct your attention to-day, for, without sharing the extravagant anticipations, often expressed, of the difficulty that we shall encounter in dealing with this problem, I nevertheless feel that the problem is a real problem and worthy of careful thought. But I do not hesitate, at the outset, to express the opinion that it can be dealt with easily and completely if we know how to use our existing banking machinery effectively. I may go further, and add that I think there is danger, if we exaggerate unduly the magnitude and difficulties of the problem, of distorting and disfiguring our banking system to its own prejudice and to the prejudice of the country's real interests.

In dealing with any problem into which so many novel, uncertain, and incalculable factors enter, it is next to impossible to distinguish between the possibilities and the probabilities, and this error, I believe, has been made by some who have been considering the problem

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of how this country will meet the export demands for gold after the close of the war. But this is not the only or the principal matter regarding which I differ with them. Granting what nobody is in a position to forecast - that there will be extremely heavy demands for gold made upon us - I feel that there is a choice of methods or means of meeting such demands to which the banking and business public should not be indifferent.

It is a matter of common knowledge that, up to date, the United States has received from Europe, since August 1, 1914, on settlement of the international trade account $631,097,000 of gold. If the present gold movement into the country sustains its pace to the end of the calendar year (as seems likely if those who estimate a trade balance in our favor of not much less than 2½ billions of dollars are right) this amount will be increased greatly. Indeed, so long as there is gold to be laid hold of, it is likely that the gold exports to us will grow (unless we take steps to check them!) because of the diminution and gradual disappearance of the supply of European-held securities marketable in this country. The result will be, indeed is already close at hand, that the United States, simply in its capacity as a trading country and without any design or ambition on its part, will have come more nearly having a control of the supply of the most fundamental and important instrumentality of modern commerce and finance than has ever been witnessed.

But the gold which the European nations have been sending us because they must now have our goods, it seems clear they will endeavor, after the war, to get back from us, because, without it, it is extremely unlikely that they could reestablish their position as trading nations.

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Problems of finance will be to the forefront in Europe because financial reconstruction must accompany, if not indeed precede commercial and industrial reconstruction. We are likely to see the experience of the United States, in the unsettled and uncertain decade following the Civil War, repeated on a gigantic scale in Europe. The vast debts piled up by the European belligerents (now estimated at close to 50 billions of dollars) the huge issues of paper currency in one form or another, make the problems of the restoration of credit, the refunding of debts, and the resumption of specie payments among the most urgent and the most difficult with which they will be confronted - problems for which no solution will be found which does not involve more or less participation and help on the side of the United States. It was well nigh ten years after the close of the Civil War before we were able to put through the successful refunding of our national debt, and it was fourteen years before we had wiped out the discount on our paper currency by the resumption of specie payments. How long the process of financial restoration in Europe will take, can not be foretold; but we may assume that, with our costly American experience as a warning example to, say nothing of the knowledge derived from some of their own past experiences, every effort will be made to shorten and hasten the process of recovery by shaping their policies and bending their energies toward the achievement. Specifically, and concretely this means that they must put an adequate foundation of gold under their inflated credit systems and their overstrained banking structures; and their chief reliance in undertaking to secure the necessary gold must be the neutral countries whose gold hoards

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have augmented so rapidly as a result of the vicissitudes of war. The Scandinavian countries, Holland and ourselves, among neutrals, and Japan among the belligerents, have been the chief recipients of the outflowing gold. All of these countries are likely, therefore, to have an opportunity to part with much of their recently acquired gold, but we are likely, yes, almost certain, to be the principal market in which the yellow metal will be sought, because of our vast holdings and acquisitions. We may also expect that the more rapid the process of financial recovery undertaken by the countries of Europe, the more intense will be the demands made upon us for gold. I repeat, therefore, that the problem of the wise and effective management of our gold supply is a very real problem.

I am not overlooking the suggestion, which has not infrequently been made within the past year by careful observers and students of the financial demoralization which is going on in Europe, that the commerce of the future will be organized upon some basis of barter and credit which will dispense with the necessity of having the liberal supply of gold necessitated under the old ways of international trading and banking. The suggestion certainly merits attention. It may be admitted that everything will be done which ingenuity, sharpened by the drastic experiences of war, can suggest, to economize the use of gold in the credit systems of the European nations. There is undeniable evidence of energetic efforts being made by the great banks of France and Germany to inaugurate a reign of economy in the handling of their gold

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by the transplantation of credit devices and expedients borrowed from the banking practice of England and the United States, such as the substitution of the checking account for the uneconomical and clumsy bank note. There is much evidence of a closer banking cooperation between the leading groups of belligerents. New and improved machinery of international settlement is being devised. This, doubtless, is one of the objects of the Economic Conference of the Entente Powers, and it is possible that some substantial and considerable changes in the gold economy of Europe will result; but it would, in my opinion be highly unsafe for us, as the leading gold holding nation of the world, to predicate our banking policies upon the supposition that gold is destined not to return to its former position of supremacy as the medium of international payment and account after the close of the war.

The history of commerce shows that banking traditions die slow and hard; and so, in my judgment, it will be with the tradition that there is but one medium of international payment which is universally valid in the modern world, namely, gold. I do not doubt that we shall get speedy and decisive testimony to this effect as soon as, or even before, the war is over. Take for example the case of Germany. Her position is in no wise different from that of her neighbors - friends or enemies - except in degree; that is, the strain upon her credit and upon her banking structure by reason of the war has been more severe, as evidenced by the magnitude of her debts and the volume of her credit circulation. Her previous position as a trading nation was the second in Europe. That trade has been completely and decisively

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cut off by the war. Germany's problem, therefore, presents only in somewhat exagerated form the situation of the other belligerent countries. All of them are straining public credit to the limit and involving the management of their great central banking institutions under the pressure of public necessity, in hazardous ventures in the field of finance. All, with the exception of England, have long since suspended specie payment - even though by one form of financial concealment or another they are attempting to mask the real situation and England herself, long renowned as the world's one and secure free gold market, is rapidly approaching the point where there will be no escape for her from a suspension of specie payment, if the war continues much longer. Such a step as the abandoment of specie payment and the dethronement of the pound sterling from its position of high prestige will be taken, we may believe, most reluctantly and as a last resort in a struggle of peculiar desperation and of national existence. And why? Because this greatest and oldest of the trading nations recognizes full well how essential gold is to the maintenance of her position in international trade and in international banking.

And so it will be with Germany and the others. No one will be quicker to appreciate than her clear-sighted economists and financial advisers, that she can not hope to recover her foreign trade without a sound system of banking and finance behind it. To invite others to trade with it, a nation must be in a position to inspire confidence in the stability and integrity of its financial system. The German mark, now seriously depreciated (estimated as much as 26%) must be brought

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back to a parity with gold. There is but one certain method for this purpose - to increase the gold supply of the country. We may expect, therefore, that no effort will be spared by Germany, England, or the other countries in a simialr position, to attain this object at the end of the war; - namely, to build up their gold supplies so as to bring them more nearly and more swiftly into equilibrium with their credit currency. Without indulging for a moment in any exaggerated fears of a so-called "gold war", we may nevertheless expect that the world will experience in an intensified form a condition analagous to that which was experienced in the decade 1870-1880, when the adoption of the gold standard by Germany and other countries, and the resumption of specie payments by the United States, Italy, and other nations, caused such a repid succession of demands for gold as to have led to its characterization, at the time, as a "scramble for gold".

The question, then, which is at once a concern to Europe and to us, is, first, where is the gold to come from, and second, what is the process by which it is going to be obtained.

The answer to the first question hardly admits of any doubt, in view of the impending loss of the position, long held and filled by England as the world's one free gold market, and in further view of the unequivocal and decisive shifting, if not for all time at any rate for a sufficiently long time, of the center of financial gravity to the United States. As a nation we now possess the largest stock of gold ever held by any single country, and we are at present the only considerable free gold market in the world. Every present indication

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is that our position in both of these ways will be cumulatively strengthened as the war goes on. It is clear beyond question, therefore, that the nations of Europe, in rehabilitating their finances, will look to the United States for gold. This question thus disposed of, the further questions for us to consider are, how is our banking organization situated to meet such foreign demands for gold as may arise, and by what process or processes may demands for our gold be expected to make themselves felt?

As regards the methods by which Europe will seek to recover some part of her gold supply, there are three which deserve notice; (1) the establishment of credits here to be taken out in gold; (2) the establishment and maintenance of discount rates sufficiently high to attract some part of our supply of floating capital, and (3) the establishment of a favorable balance of trade, which would require gold remittances by us. The successful flotation in the American market during the past two years of foreign government issues may have be - gotten the expectation that considerable loans can be placed here on the return of peace; and such may be the case for a short time and for loans of a special character and of limited amount. But it is not probable that any such method of taking gold from us could obtain large dimensions or last very long. It is probable, however, that for a while at least, some of our floating funds might be diverted to the European market by higher discount rates. If such a shifting should attain undesirable dimensions, however, it could easily be controlled by raising our own rates. European countries desiring gold from us

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will, therefore, have to rely mainly upon the natural processes of trade. Just as England and other countries have parted with enormous quantities of securities and gold to us because of their unfavorable balance of trade, so it will be by reversing the process and establishing a balance of trade in their favor that they will be most likely to succeed in "repatriating" their lost gold.

A country in times of peace can not, of course, be forced to part with its gold except by commercial pressure or inducement; in other words, except as it is its interest and advantage to do so. That will be when its gold has a higher value in a foreign market than it has in the home market. Prices and discount rates are the chief agencies through which gold distributes itself in proportion to normal commercial requirements among the gold-using countries. Gold will leave this country because, and to the extent, that gold prices are higher here than elsewhere, or discount rates lower. We may expect that after the war prices for staple commodities in the leading world's markets will find their new level gradually, and that gold will distribute itself so as to maintain prices in the different countries in conformity with the new price level. It is possible, and is probably a contingency not to be overlooked, that a replenishment of gold stocks may be so essential to some of the European countries that they will attempt by artificial means, (that is, through the stimulation of exports and by high discount rates) to establish the balance of trade in their favor. No doubt some such view or fear as this is in the minds of those who believe, or profess to believe, that so-called "raids" will be made upon our gold supply by means of "dumping".

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ought, of course, be in a position to protect ourselves against any such artificial methods of trade should occasion arise, and for this purpose, as well as other purposes, have wisely created a tariff commission. But I venture to suggest that such anticipations are not to be taken too seriously.

No one can foretell what changes in the competitive capacities and relative positions of the leading trading nations as debtor and creditor will result in the economic and financial readjustments that will follow from the war. It is easy to draw a picture of Europe industrially exhausted, prostrate, and helpless after the war, and requiring many years for recovery. It is equally easy to conceive a Europe emerging from the trenches made strong, resolute, and formidable by the hard discipline of war. There will no doubt be elements both of strength and of weakness in the economic capabilities and recuperative powers of Europe's industrial leaders. Which way the balance will tip in the case of particular countries, no one can foresee. What is, therefore, important for us is that, while carefully watching developments and signs, not to make the error on the one hand of exaggerating the difficulties with which we shall be confronted, nor, on the other hand, of minimizing the possibilities which attach to the situation.

My own view and expectation is that the United States may be expected for a long time, perhaps permanently, to hold the position of a creditor nation, to which she has attained during the war: first, because of the practical extinction of our financial obligations to

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Europe, the interest on which had long been a very important element in the international account; secondly, because of the considerable financial obligations that Europe has incurred to us; and thirdly, because industrially and commercially our position as the leading source of supply of many of the most important requisites of commerce will be strengthened by reason of the depletion of stocks of raw materials, etc., in Europe, and because the "forced draught" which war orders have given to the establishment and expansion of many of our leading manufacturing industries has given an impulse to our outward commerce which is likely for years to lead to a mass and value of exports which will pay or more than pay for all the goods and services we shall need from Europe. Indeed, it is conceivable that a situation may exist for some considerable time after the war in which the problem will be rather how to get rid of some of our redundant gold advantageously, than how to hold on to it.

We now have more gold than we need. The hard necessities of war have obliged Europe to send us gold in excess of our normal and proper requirements. Prices for commodities generally have been driven up by leaps and bounds. There are many things that we need from Europe much more than we do gold, and in return for which we should be glad and ready to part with our surplus stock of gold. Good financial policy on our part will, therefore, be directed not toward undertaking to make provision <u>against</u> a return of gold to Europe, but toward making provision <u>for</u> its return by a gradual, orderly, and well-controlled process. This problem, I repeat, which has inspired a

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feeling of great anxiety and even of alarm in some, really presents no difficulties which we can not easily master, even if we assume that the problem may be one of very much larger dimensions than there is now good reason for expecting.

What dimensions the gold movement to Europe may be expected to attain to, we can only conjecture. Whether, in the course of time, we shall return to Europe all the gold that we have received from her may be doubted; certainly not for some considerable time. We shall not, therefore, be erring on the side of under-statement of the possibilities of the situation, if we assume that the maximum amount of gold which we may be called upon in time to send back to Europe, will be approximately equal to what we have received.

Thus far, we have received since August 1, 1914, $631,097,000 more gold than we have exported. If we assume, further, that the rapidity with which the return will be made will be approximately identical with the rate of rapidity at which we have received it, we should be far within the limits of safe calculation if we fixed upon some $500,000,000 or $600,000,000 at the present time, as the gold export demand which the banking system of the country might be called upon to meet within a period of two years. If the war runs another year, we may have to take more millions of European gold and might have to raise correspondingly the approximate amount of gold which might have to be returned to Europe. I say "might" rather than "would", because of my firm expectation that we shall not have to

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return so large an amount, and also because I realize the importance of being prepared to deal with possibilities, in the face of so unprecedented a situation, however remote the possibilities may seem, and finally because of my strong conviction that there is nothing whatever in the possibilities which need embarrass us. Assuming, then, that we may have to return in the course of some two years, some $500,000,000 or $600,000,000 of gold, how is our banking machinery prepared to cope with the problem of its orderly management?

This problem is one which concerns every part of our American banking system. But it may be admitted that it is in a peculiar sense a problem of concern to the Federal Reserve System. The Federal Reserve Banks were specifically created, among other important objects, to manage the banking reserves of their members and to regulate the movements of gold.

What, then, is the gold position of the country and of the several component parts of its banking system, and especially, what is the gold position of the Federal Reserve Banks?

The total gold holdings of the United States at this time, are estimated at $2,600,000,000. Of this amount, approximately $280,000,000 is in the Treasury of the United States, the balance being distributed amongst the banks of the country, including the Federal Reserve Banks, and the hands of the general public. Over $500,000 is held by the member banks of the Federal Reserve System, over $300,000,000 is estimated to be held by State banks and trust

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companies, and the rest, it may be conjecturally estimated, is in the hands of the general public. The total amount of gold held in and by the Federal Reserve System is $616,000,000. (October 13, 1916). This is made up of $406,000,000 held by the Federal Reserve Banks, and $210,000,000 held by the Federal Reserve Agents, this last being some of the redundant gold of the country which has been impounded in exchange for Federal reserve notes, and which is in the keeping of the Federal Reserve Agents, to be held until the occasion for its use arises. It should not be inferred, however, that all of the $616,000,000 held in the Federal Reserve System is free gold available to meet a foreign drain. Certain deductions must be made in arriving at a statement of the Federal Reserve System's free gold assets. The most important deductions are the reserves of 35% required by the law to be held against the reserve deposits of member banks, and of 40% against outstanding Federal reserve notes. These deductions now aggregate $195,000,000. After allowing for these reserves, and, in addition, for a 40% reserve against Federal reserve notes now secured by gold in the hands of the Federal Reserve Agents which could be replaced by the deposit of eligible commercial collateral to secure such notes, the amount of the Federal Reserve System's available gold may be set down as $345,000,000.

(In November of this year, a further installment of member bank reserves will be deposited with the Reserve Banks, to an estimated amount of about $60,000,000. If this should all be deposited in gold, the free gold holdings of the Federal Reserve Banks, after allowing for the required 35% reserve against the new deposits, would be increased by $38,500,000, bringing the total free gold of the system to over $380,000,000.)

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Gold Lending Power of Federal Reserve Banks.

(Without calling in money invested in open market purchases of commercial) (paper and municipal warrants)

Condition of all Federal Reserve Banks at close of business Oct. 13, 1916.

Items (In thousands of Dollars)	As published	After (1) redeeming Federal reserve notes on hand, and (2) deducting from deposits the amount "Due from other Federal Reserve Banks
Assets:		
Gold and lawful money	405,725	424,483
Bills discounted:		
For Member Banks	22,099	22,099
B't in open market	77,387	77,387
U.S.Bonds & Notes	53,086	53,086
Municipal Warrants	31,542	31,542
Federal Reserve Notes	15,280	------
Due from other Federal Reserve Banks	30,089	------
Other assets	3,045	3,045
	638,253	611,642
Liabilities:		
Capital paid in	55,682	55,682
Deposits:		
Gov't. 24,715		
Bank 544,043	568,758	538,669
F. R. Notes	12,316	15,794
F. R. Bank notes in circulation	1,033	1,033
Other liabilities	464	464
	638,253	611,642
FEDERAL RESERVE AGTS:		
Fed. Res. Notes:		
In circulation	207,124	207,124
Held by F.R.Bks.	18,758	-------
Issued to the banks	225,882	207,124
Gold held to retire F. R. Notes	210,088	191,330
Commercial paper held as collateral for Federal reserve notes	15,794	15,794
	225,882	207,124

Amount of gold available after setting aside all required reserves.

Gold held by Banks	424,483	
Less required reserve of .35x538,669= 188,534		
.40x15,794 = 6,317	194,851	
Available		229,632
Gold held by F.R.Agents	191,330	
Less reserve which would be required were commercial paper substituted as backing for the Federal reserve notes now covered by this gold .40x191,330=	76,532	
Available		114,798
Total Free Gold		344,430

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$345,000,000 of free gold is certainly an imposing aggregate. It is the largest amount of gold that has ever been massed under effective and unified banking control in this country. To many it will seem altogether sufficient to answer any probable needs. Indeed if we were to be guided in our judgment of the probable provision that should be made, purely by our past experience, and neglect the profound changes which have come to pass in the world of finance during the past two years, we might well believe that this amount would not only be ample but more than ample, easily to provide for any probable demands. But I have already stated my reasons for believing that it will be prudent, in making our calculations, to take note of the possibilities as well as the probabilities, particularly as the latter are so incalculable, and to accept $500,000,000 or $600,000,000 as the figure to bear in mind in estimating the amount of the possible gold demands that might be made upon us. Taking this figure as the goal of our calculations, it is clear that the present resources of the Federal Reserve System, big as they are, are not to be regarded in any but an optimistic calculation as certainly equal to meeting any possible drains of gold that might develop at the close of the war, and be equal, at the same time, to supplying any needs of our domestic banking situation which may develop. The practical problem confronting the managers of the Federal Reserve System is, therefore, how best to proceed in undertaking to mobilize from the extensive gold supply of the country outside of the Federal Reserve System, an amount of

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gold which will bring the free holdings of the System up to, say $500,000,000 or $600,000,000; that is to say, how to bring under the control or management of the Federal Reserve Banks an additional potential of $400,000,000 of gold, of which $260,000,000 would be over and above the required reserves.

This looks like a big order, but this is a day and a country of big things, and we are equal to the order. The problem should offer no great difficulty if we are alive to its importance, for the $400,000,000 additional gold required by the Federal Reserve System is but one-sixth of the country's total supply. The problem has had the careful attention of the managers of the Federal Reserve System, and in its general aspects had the attention of the Congress which enacted the Federal Reserve Act; for while such a sensational contingency as that with which we are now confronted could not have been foreseen when the Federal Reserve Act was framed it was foreseen that situations which would call for an effective marshalling of our gold resources would arise, and many of the fundamental features of the Reserve System were shaped with reference to this requirement; for the problem of handling the country's gold supply is, in a very special sense, a problem in reserve banking.

In England, France, and Germany, the marshalling and handling of the gold supply has long been regarded as the problem and responsibility of the great central banks, and the methods approved in their experience and practice will be our best guides in finding the solution for our problem, if we know how to make a discriminating

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application of their experience to our conditions. And because the general banking habits of our country parallel those of England much more closely than they do those of continental Europe. it would seem that in developing our banking machinery for the purpose of managing the gold export problem, the analogy of the Bank of England rather than that of either the Reichsbank of Germany or the Bank of France would be the one most likely to suggest or indicate the methods to be followed by us; all the more, as England's banking methods were developed in connection with the position long successfully maintained by her as the world's one free gold market - a position and responsibility which there are good reasons for believing may henceforth be ours.

The main difference between the banking methods of England and of continental Europe concerns their habits with respect to the use of the bank note and the bank check. The central banks of France and Germany are primarily note-issuing banks, deposit credits holding a very unimportant, almost a negligible, place among their liabilities. The bank note is their most characteristic form of credit, the means by which they build up their gold holdings, issuing their notes in exchange for gold and then holding the gold among their working assets. Without the note they cound not function.

In England, the situation is very different. There, the bank note has a very subordinate place, and as a form of currency

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is rapidly growing obsolete. It was long since effectively superseded in the preference of the English banking community by the deposit and checking account. The Bank of England issues no credit currency. Its notes are practically bullion certificates, and yet the Bank of England sustains a more intimate, vital, responsible and strategic relation - as a reserve holding bank - to the whole banking and credit structure of England than that of any other of the great central banks. The great joint stock banks of England have long recognized their dependence upon the Bank of England, and maintain the larger part of their banking reserves with the Bank of England in the form of deposit credits. How successfully this system has worked, is one of the proudest chapters in the history of British banking, and it was this system which the framers of the Reserve System had in mind when they provided for the establishment of a similar relationship between the banks of our country and the Federal Reserve Banks; with this difference, that the deposit of a certain percentage of the banking reserves of the member banks with the Federal Reserve Banks, was made a legal requirement instead of being left to the voluntary action of the banks.

The Reserve Act originally provided, after the shifting of reserves incident to the establishment of the Federal Reserve System is completed in November 1917, for the maintenance of reserves by the banks of central reserve cities, reserve cities, and so-called country

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banks, respectively, in the following percentages, with their Federal Reserve Banks:- 7/18ths, 6/15ths, and 5/12ths of their demand deposits. A certain percentage of the balance of their reserves, after November 1917, they were, by the terms of the original Act, to be required to carry in their own vaults, as follows; 6/18ths for central reserve city banks, 5/15ths for reserve city banks, and 4/12ths for country banks. The remainder could be carried at their option either in vault or at Federal Reserve Banks. If the requirements I have stated my reasons for believing the Federal Reserve System might be called upon to meet are reasonable, it would appear that the disposition of the reserves of member banks originally made in the Act may not put the System in a sufficiently strong position in view of the new circumstances in which the country is finding itself as a result of the war. The logical and natural course to follow in meeting the situation would seem to be a further development of our scheme of Reserve Banking along the lines originally laid down in the Federal Reserve Act; that is, by providing for a larger concentration of the cash holdings of the national banks in the Federal Reserve System.

Provision to accomplish this purpose was, therefore, wisely made by Congress in the recent amendments made by it to the Reserve Act, in an amendment which relieves member banks henceforth of the necessity of holding any fixed percentage of their legally required reserves in vault, and by leaving them free to carry such portion as they see fit with their Federal Reserve Banks, thus opening a natural way of adding to the cash holdings of the Reserve Banks. A similar

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result could, of course, have been reached by introducing into the Federal Reserve Act a freer system of note issue by the Reserve Banks patterned after the model of the German or French systems, but such a solution would, in my judgment, be attended with such grave dangers and be so ill adapted to American banking conditions and practices and the fundamental principles of our system of regional reserve banking that it could not but be viewed with serious misgiving by those who appreciate that the note issue system of the Federal Reserve Act makes every reasonable provision for the issue of an elastic bank note currency without inviting its abuse. I therefore regard the recent amendment to the Reserve Act allowing the member banks to increase their reserve deposits with their Reserve Banks, without limitation or restriction except such as their own judgment of their interests and necessities may impose, as one of the most important steps that could have been taken in the further development of the Federal Reserve System. It provides a simple, direct and natural way of strengthening the Reserve Banks as that becomes necessary, and forestalls any occasion for resort to alternative methods of doubtful expediency.

The situation in which we now happily find ourselves as a consequence of the opportunity thus given for the development of a closer relationship between the Federal Reserve Banks and their member banks, is that the American banking system, of which the Reserve Banks are the very heart and center (as managers of the country's banking reserve) can be made as strong for handling the problems and conditions which may confront us, as you member bankers are willing to make it.

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I repeat with all emphasis that the object of this new provision of the law allowing, but not requiring, the deposit of member banks' vault reserve money in their Federal Reserve Banks, is to strengthen the gold position of the Reserve Banks. I do not doubt that it can be so used as to afford an effective solution of any gold problem which may confront us. Without any inconvenience or risk to themselves, without unduly trenching upon their cash holdings in vault or till, the member banks of the Federal Reserve System can easily spare the amount of cash which will be necessary to bring up the free gold holdings of the Federal Reserve Banks at the present time to $500,000,000 or $600,000,000.

The National banks to-day have cash holdings of over $750,000,000. State banks and trust companies outside of the Federal Reserve System are estimated to hold upwards of $330,000,000 in gold. How much longer State banks will delay in entering the Federal Reserve System can not be foretold, but they are not likely to find their position on the outside of the Federal Reserve System a very comfortable or reassuring one, when the financial readjustments at the close of the war are under way. Accessions to the State bank membership of the System are then likely to become the order of the day. The larger the membership and the resources of the banks composing the Federal Reserve system, the easier, of course, will it be to provide the $400,000,000, more or less, which the Federal Reserve Banks will require in order to bring their free gold holdings to $600,000,000. But even supposing that the whole burden would have to be borne by the present mem-

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bership of the System, the required addition to the Reserve Banks' gold could be provided and yet leave the banks with over $350,000,000 of till money. The member banks in the three central reserve cities alone hold $340,000,000 of cash which would enable them to part with $246,000,000 to their Federal Reserve Banks and yet hold in till an amount ($97,000,000) equal to 3½% of their deposits. When it is added that the central reserve cities and many of the reserve cities of the country are either Federal Reserve Cities or else near Federal Reserve Cities and are therefore in close contact with their Federal Reserve Banks, it is evident that they would have no difficulty in keeping themselves supplied with till money should their requirements run beyond the estimated 3 to 5 per cent. English experience has shown that in countries where the checking account is the customary method of payment, banks can in all ordinary circumstances run along safely with till money averaging about 2% of their demand liabilities. If the shifting of cash would be promoted by a change in the form of your condition statement which would show your cash in vault and in the Federal Reserve Bank as one item I see no good reason why this should not be done and could not be done.

The further solution of the problem is, therefore, in your hands. We have a splendid piece of machinery in the Reserve System, and you have it in your hands to make it an engine of gigantic power for handling, as an orderly and well-controlled process, any gold export movement that may set in, by bringing your spare cash to your Federal Reserve Banks, as the law contemplates you should and will do.

It is, of course, conceivable, though extremely improbable, that a gold export movement after the war might develop which would call for a larger provision than what I have thus far taken as the basis of

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our calculations. To many it will seem so improbable as hardly to merit attention, but I have stated why we should be prepared to deal with possibilities. It should not, therefore, be overlooked that there are methods of tapping the community's extensive holdings of gold which are outside of the banks, and in any event let us not lose sight of the fact that gold lost by the banks to meet a foreign drain would, in the natural course, be replaced from the community's holdings quite speedily. Only the first impact of a foreign demand for gold would be felt by the banks. The ultimate incidence of such a demand would be the now superabundant gold stores of the community. Gold holdings in the hands of the general community are estimated, at the present time, to amount to the huge aggregate of $900,000,000, and dissatisfaction is not infrequently expressed with the fact that our circulation should be so substantially made up of gold in the pockets of the people instead of being replaced by some form of credit currency. But the experience of the greatest trading and banking nations shows that a solid substratum of gold in the general circulation of a country is one of the surest foundations of a secure banking and financial system. It is wrong to assume that gold thus distributed in the channels of circulation can not be effectively mobilized when occasion arises, and be drawn into the banking reserves. The European nations in recent months have given us some impressive examples of such mobilization. I believe that the floating gold supply of the United States is a matter quite largely within the control of the banks of the country, and that the banks will exercise that control in their own interest and in the interest of the country, as it becomes necessary

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The moment that gold grows in demand for the purpose of meeting foreign shipments and replenishing reserves, banks which are now indifferent or careless as to whether they pay out over their counters in response to currency demands, gold certificates, National bank notes or Federal reserve notes, will begin to discriminate. They will segregate their gold certificates, and as the withdrawal of these from general circulation reduces the volume of the community's necessary currency, the banks will find it to their interest to meet counter demands for cash by taking out Federal reserve notes. In other words, gold and gold certificates will be reserved for such uses as can not be met by the Federal reserve notes - to wit, meeting a foreign demand for gold, or increased bank reserves - and the Federal Reserve currency will be substituted to the extent that the circulating medium of the country requires it. Because at the present moment we are the only considerable country that is on a gold basis and have acquired on settlement of the international trade balance a volume of gold that has made gold so redundant in this country that gold certificates are for the moment a cheap medium of circulation, we should not hastily assume that changed conditions will not reverse the process and lead by natural and inevitable means to a substitution of the Federal Reserve note in large measure for the gold certificate. The whole question of the attitude to be adopted in the matter of the control of our gold supply turns upon whether we shall continue to have faith in the natural and normal processes of money and trade, or whether we are going to allow ourselves to be frightened into assuming that things

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have so changed that those processes are going to fail, and that henceforth we shall have to resort to artificial shifts and manipulations.

You bankers know how rapidly currency circulates in this country - more rapidly, in fact, than it does in any other country of the world. It is a familar fact that the American bank check is a highly flexible medium of credit, but the velocity of movement of ordinary bank or Government currency is not so highly appreciated. The fact is that these turn over with marvellous frequency compared with such countries as France, or even Germany, where the movement of the bank note is sluggish; in part because large quantities are carried idle in the pockets of the people or are locked away in the strong-boxes of shop-keepers. The turn over of the average piece of paper currency in the United States (outside of banks and the United States Treasury) has been estimated as high as twenty-two times in a year. You bankers also know as a matter of daily experience that the channels through which the paper money of the United States circulates, lead into and out of the banks, so that in the course of a year, practically the whole volume of the country's paper currency passes through the hands of the banks many times. It is therefore no unwarranted assumption to conclude that the banks have it in their power easily to withdraw the gold certificate from circulation and to substitute the Federal reserve note, when conditions indicate such a course to be desirable or necessary. In brief, in a country whose habits with respect to the circulation of the bank note are what they are in the

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United States, the mobilization of a very considerable part of the gold currency of the country in a comparatively short period of time is a matter easily within the banks' power. This is a fact of such fundamental importance that it must not be neglected in estimating just what could be done in developing and making effective a policy to mobilize the gold supply of the country.

Nor should we overlook the extraordinary ability of the country to protect itself against any violent loss of gold by using for this purpose some part of the extensive holdings of European securities which we have recently acquired. To date, we have purchased European securities to the extent of $1,227,000,000. These are all of short maturity, the amounts maturing in the years 1917 and 1918, which presumably will see the close of the war, amounting to no less than $360,000,000.

MATURITIES OF EUROPEAN OBLIGATIONS HELD IN THE UNITED STATES.

1916	$30,000,000
1917	103,000,000
1918	260,000,000
1919	150,000,000
1920	500,000,000
1921	50,000,000
1923	5,000,000
Uncertain	129,000,000
	$1,227,000,000

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The events of the past two years have shown that American securities of undoubted solidity possess the quality of international currency, and are likely to figure to an important extent in the settlement of international accounts between this country and Europe. The great extension of the international loan market which has been one accompaniment of the war is certain to result in a greatly enlarged use of acceptable securities as a means of international payment and as a substitute for gold in making international settlements. There is every reason for believing that the recent experience of European countries in converting their American securities into gold have given to these securities an enviable position as secondary bank reserves, and that this will insure the reappearance of some demand for American securities after the war, thus broadening their market and facilitating their continuing use as a medium of international payment.

But, finally, let us not overlook the powerful instrument of control which the Reserve Banks possess in a movable discount rate for protecting their own and the country's gold supply, should it be threatened with too large or too sudden a foreign drain. This is the method employed by the great reserve and central banks in England and Europe. It is in particular the method, the use of which has been most effectively developed and extensively applied in England, whose money market has been more exposed than that of any other country to foreign demands for gold, because of her extensive and intimate commercial relations with the world, and because of her position as the

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world's principal gold market. Whenever the Bank of England has found that gold is being drawn out of the London market too rapidly, it has raised the bank rate so as to make the process of withdrawal more expensive, and thus to temper it to what the banking situation could stand. This method has been so frequently employed that a rise of the bank rate is commonly regarded as the most accurate barometer of the English reserve situation. And it is also the means by which the Bank of England exercises a strategic control over English banking at times when such control is all-important.

In the twenty-five years between 1875 and 1900, the English bank rate was altered 167 times, which means an average duration of the same rate, of only 54 days. Indeed, not only were changes of rate frequent, but their range was also considerable - such as four or five percent of variation in the course of a year. This same instrument of control, our Reserve Banks possess, and the success of our new banking system will in large measure depend upon the wisdom and skill its managers and the Federal Reserve Board develop in handling it.

It must be admitted that frequent changes of discount rates are in and of themselves not desirable. Stability of rate is a great advantage to industry and the internal banking situation, but too much stability of Reserve Bank rates must not be expected in a country whose money market has attained the international importance which ours has, at least for the present, and which it will continue to hold so long as its position in international trade is that of a creditor, and so long as it has a vast stock of gold to be dispensed. At any rate,

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whatever internal disadvantages may attach to a changeable discount rate, there it is, a powerful weapon for exercising a control over the reserve and gold situation by the Federal Reserve Banks at critical times, and should not be omitted from our calculation when examining our protective capacity against an undue drain of gold. It would be an especially effective and necessary weapon against any attempt of European markets to bid away gold from us more rapidly than would be consistent with our interests, by raising their discount rates.

More than that, it would be an effective method by which the Reserve Banks could throw upon the many powerful banks of the country which have large holdings of cash and foreign commitments, their proper part of the burden of supplying gold for foreign shipment, should they be unduly disposed to divert demands made upon them to the Federal Reserve Banks. Indeed, demands for foreign gold remittances would make themselves felt in the first instance as a demand by customers of these banks. To meet such demands, they would have the alternative of taking the gold out of their own accumulations or of drawing it out of Federal Reserve Banks by rediscounting or open market sales. But it is not to be expected that the Reserve Bank managers would sit idly or carelessly by and allow their gold reserves to be needlessly depleted, when they could stop such depletion by the simple device of raising their rates, unless, or until, a situation had arisen which was beyond the ability of the ordinary banks to handle with their own resources and without difficulty.

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This survey shows that there are many elements that enter into the problem of handling our gold supply and many factors that enter into the organization of the machinery for most effectively mobilizing it. It may be convenient before dismissing the subject to assemble them in a summary statement. They are:

1. Europe may be expected in time to recover a large part of the gold she has sent us. There being no present method of estimating the probabilities, attention must be paid to the possibilities.

2. Europe having sent us thus far over $630,000,000, prudent calculations will address themselves toward considering how an amount of $500,000,000 or $600,000,000 of gold might best be mobilized for the purpose of meeting a foreign drain should it attain such a magnitude.

3. The Federal Reserve Banking System, including therein the member banks, possesses over $1,366,000,000 in cash, of which over $1,100,000,000 is gold (which is something short of one-half of the total gold supply of the country), the remainder being exchangeable for gold at the Treasury of the United States.

4. The total gold within the immediate control of the Federal Reserve Banks amounts to $616,000,000, of which $345,000,000 may be regarded as free gold; that is, the amount of gold lending power without any impairment of reserves.

5. To raise the gold lending power of the Reserve Banks to the point which would be necessary to enable them to meet (what is, however,

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in view of present probabilities unlikely) possible demands of $500,000,000 or $600,000,000, approximately $400,000,000 would have to be added to the Reserve Banks deposits in order to give them, after setting aside the necessary reserve of 35%, additional free gold to the amount of $260,000,000.

6. This amount can be spared from vault cash now carried by member banks without unduly reducing their holdings of till money, and therefore presents the basis for the solution of the problem.

7. Gold lost by the banks to meet foreign demands would be replaced by mobilizing a part of the present floating supply of the community into their hands. This process would be facilitated by the ease with which Federal reserve notes could be issued to fill the void created by the withdrawal of gold or other forms of currency.

8. The Reserve Banks possess an important leverage of control in their movable discount rate, which could be adjusted to counter any undue attempt of foreign markets to attract our gold by high rates.

9. An important element of strength in the protective capacity of the country against an undue drain of gold is the heavy holding of foreign government obligations which run off in the next few years.

10. Finally, while realizing the importance of being alive to the possibilities in the face of a situation for which there is no parallel, let us not make the mistake of "overtraining" or of committing ourselves in advance to any definite single expectation of what is going to occur and in consequence lose that balance of judgment which will not hesitate to shape and reshape its conclusions

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in accordance with the facts as they develop or change. An essential element in our preparation will be the ability to deal with the unexpected as well as with the anticipated.

The conclusion warranted by this survey is that the Reserve Banks can easily, with the cooperation of their member banks be put in a position where they can master any situation which may arise. Some of you may say that it is a heavy bill that I am proposing the Federal Reserve System shall draw on you, but this is the day of the bankers' acceptance in our new American banking system, and I feel confident, from the hearty cooperation that our member banks and the country by and large are giving to the Federal Reserve System, that you will not protest the draft but accept it. The bankers of the United States had to meet several severe tests in the trying months following the outbreak of the great war. Those tests they met intelligently and resolutely. I do not doubt that this one also will be met intelligently and resolutely, and that each one of our members will take careful reckoning of what he can do and do it. The Federal Reserve System is but two years old, a brief period in the life of a great and new banking experiment, but the system has already made a record for itself and an enviable place in our new financial and credit system, and is no longer an experiment in the sense that there is any uncertainty as to its high value and entire practicability. It is experimental only in the sense that there may be a question as to how

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rapidly it will develop its full potentialities as the shaping and guiding influence in American banking affairs.

A great banking system is as much a matter of growth and development as it is of legislation. The English banking system, which has long been the admiration of the world, has grown up pretty much without legislative guidance or interference. The Federal Reserve Act, wonderfully conceived as it was, is, therefore, to be regarded only as a beginning. It presents an opportunity. How fully the opportunity will be improved to develop a great system must depend upon the combined wisdom and vision of those of us immediately charged with the administration of the law, and the thousands of you bankers who are the partners through whom and with whom we must work. A banking system is not a set of principles and rules formulated and imposed by law, but a set of habits, practices, customs and traditions forged out of experience. Many of these that are excellent we already possess, but others we still must make. I have pointed out one of the most important of these. Our country has become a dominant factor in the world of commerce and the world of finance. Our banking system must be made equal to our matchless opportunities and our large responsibilities. Whether we like or desire the great changes which have come to pass in our position in the world of affairs makes little difference; we are there by fate and circumstance and we must cultivate the habits of thought and action which will enable us to do our part and do it well. Parochial habits and provincial customs

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must yield to the larger way of viewing things and the larger way of doing things. This is the day of banking cooperation and the Federal Reserve System is your rallying point in helping yourselves and helping the country. It is the best rallying point that banking wisdom and legislative ingenuity have ever given the bankers of any country, and is worthy of your every confidence and support.

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F E D E R A L R E S E R V E N O T E S .

The proposition to meet the gold export problem by changing the character of the Federal reserve note has been made with such frequency and with such earnestness of conviction in high quarters recently, that it can not be ignored. Complaint is made by those who criticize the system of note-issue established by the Federal Reserve Act, that the Federal reserve notes are subject to unnecessary and burdensome restrictions with respect to their issue. What, then, is the existing method of issue, and how is it proposed to alter it?

Following the analogy of the Bank of England, which separates the Issue Department from the Banking Department, the issue of Federal reserve notes is made by the Federal Reserve Agent, representing the Government, to his Federal Reserve Bank, the bank desiring the issue pledging satisfactory commercial collateral as an evidence that the issue is needed and as security for it. The further provision restricting note issues is the familiar one that a minimum reserve of 40% in gold or lawful money must be maintained by the bank against all issues outstanding from it, the purpose of the latter being to insure the prompt convertibility of the note under all probable circumstances and to insure that the issues of Federal Reserve Banks shall always be in some reasonable proportion to the gold assets of the banks. Convertibility and requisite character of security - as evidencing the need of the issue, - are the two first essentials in any elastic bank note

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currency, the third essential being adequate inducements to redemption. This last, the Reserve Act undertakes to secure, first by the provision that no Federal Reserve Bank shall pay out notes of another Federal Reserve Bank, but promptly return them to the issuing bank for redemption, and second, by not permitting Federal reserve notes to be used in the reserves of member banks. This last named restriction has sometimes been criticized as a serious limitation upon the usefulness of the Federal reserve note, but it was manifestly conceived in the interests of elasticity.

What our American system of credit currency lacked was an elastic element. To contribute this element, the Reserve Act provides not only a natural and almost automatic method of issuing the notes, but also an almost equally automatic method of their retirement. The mere fact that the reserve note has no use except as a medium of exchange is the best guarantee that when such notes begin to accumulate in the hands of the banks, they will be returned by the banks to the Reserve Banks for redemption, and thus there will be an automatic ebb and flow of the reserve note issues to and from the banks in response to the seasonal variations in the country's currency requirements, such as could not have been expected or attained if the reserve notes had been clothed with the full character of money and been permitted to count as money in the reserves of member banks.

An elastic credit currency always involves the danger of

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overissue. The problem of legislative regulation is, therefore, while giving every possible facility for issue in response to actual commercial needs, to restrict the temptation to make issues not needed by the current convenience of the community; that is, to provide against overissue by not allowing too wide a margin for the exercise of discretion by the issuing bank. Barring certain cumbersome features in the machinery of the Federal reserve note issues (for which, however, experience has found or is finding a solution apart from any considerable changes in the law) the unique excellence of the note provisions of the Federal Reserve Act is to be commended as providing a maximum of elasticity with a minimum of danger of overissue. But however important an elastic element in the note currency of a country is, and however appropriate an agency for the issue of such currency the Federal Reserve Banks are, it should nevertheless be emphasized that in a country where the vast mass of business transactions is effected not by means of note currency but by means of check or deposit currency, note issue is a mere incident in reserve banking. In continental Europe, the account current and the bank check are not much used, the habits of their business communities marking the bank note as the form in which they prefer to use banking credit. Unlike the great central banks of continental Europe, our Reserve Banks are not primarily note-issuing banks. Their primary function is to provide credit in the typical form customary not only among banks but in the business community at large, namely the form of deposit credit. Restrictions, therefore, imposed by the Federal Reserve Act upon note issues in the interest at once of safety

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and elasticity, which might prove burdensome in countries where the principal business of the banks is to issue bank notes because of the small volume of their credit which the community will use in the familiar form of the checking account, are of little or no inconvenience with us.

On the other hand, the danger of ill-controlled issues - not to say overissues - is far from being an illusive one. Over-issue - or let us frankly use the less agreeable word "inflation" - has at one time or another always overtaken the credit currency of countries that have been restive under restrictions upon bank note issues. Such inflation has been going on during the last two years at a breakneck pace in the two countries of Europe which have the monumental central banks of issue, namely, France and Germany, and there is food for reflection in the energetic efforts that they have both latterly been making to counteract some of the effects of their policy of note issues by undertaking a systematic campaign of education for the purpose of inducing, in measure, the substitution of the checking account for the bank note. (Note the recent brochure of the Bank of France on this subject).

In flush times when all goes well, we are apt to minimize the possibilities of inflation, and it is easily said that, of course, under any change in the status of the Federal reserve note by which it will be given the more definite character of a note issued against

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the general credit of the Federal Reserve Banks, the banks will be expected to, and in fact will, carry reserves not of the minimum of 40% established in the law, but of 70% or more. It is easier, however, to formulate a counsel of perfection than it is to insure its observance, and so it would probably be with this one. Ours has long been a country of fixed reserve requirements. The banker's mind and habits in America have been developed under the so-called legal or minimum reserve requirement, and bankers of nearly every degree, inevitably and in spite of themselves, or of any resolve that they may make to the contrary in times of piping peace, or that anyone may undertake to impose upon them, will work to the legal minimum as a boundary of legitimacy in determining the range of their credit operations. We may expect that the managers of the Federal Reserve Banks will be immune to many of the temptations that beset the path of the ordinary banker, responsible, as he thinks, to himself alone; but it is also well to recall that when the Federal Reserve Act was on its passage in Congress, the fear was not infrequently expressed that the Federal reserve note, even carefully guarded and restricted as it was against abuse in the Federal Reserve Act, was nevertheless exposed to the danger of too easy issue.

As a matter of fact, we have had no inflation of Federal reserve notes, rather the reverse has been true; but that is no reason why we should be willing to consider relaxing the reasonable safe-

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guards of the Act, and, simply for the sake of making the reserve note a more pliable instrument for drawing gold into the Reserve Banks, expose it to the risk of deterioration. That such a method of note issue would provide an easy way of obtaining the community's floating gold to the extent that the community would be willing to accept the note in exchange for gold, may be admitted; but it is also clear that such a method of issue would constantly carry with it the possibility of inflation - a possibility not to be taken too lightly in a country whose business temper is most frequently apt to be either one of high optimism, seeking nutriment and support in the way of abundant credit, or else one of severe pessimism and despair, seeking sympathy and comfort in the way of easy credit. When we observe the rapidity with which this country has absorbed the enormous volume of credit created by the release of banking reserves under the organization of the Federal Reserve System, and the added volume created by the accession of large supplies of foreign gold (since August 1, 1914, to date, we have received $631,097,000 more than we have exported), we get some idea of the capacity of the American appetite for credit. The fact is that an American business community can always be counted upon to live up to the possibilities of its credit, and it is no exaggeration to say that we are at this moment in the midst of a career of credit inflation.

On the other hand, a review of American banking and currency history shows that hard times have seldom failed to produce

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the suggestion of cheap and easy money as the remedy. When I recall the insistence with which, during the sombre first months following the beginning of the European war and the temporary breakdown of trade with Europe, the Federal Reserve Board was urged to join in supporting a proposition for an issue of $500,000,000 of Government currency for the purpose of stabilizing the nominal value of staple crops, and of making National bank notes legal reserve money, I can not lightly brush aside the danger of note inflation as one not seriously to be reckoned with any longer in the operation of American banking. There are some forms of temptation and illusion that beset poor weak human nature even in so enlightened a business country as ours, when the opportunity seems sufficiently alluring or the emergency sufficiently overwhelming. At any rate, the menace of overexpansion which would constantly lurk among the possibilities of the Federal Reserve System under a system of freer note issue than the present one, would, in order to be effectively controlled, involve the necessity of such close and highly centralized control of the Reserve Banks, as would, in my opinion, mean practically the destruction of much of their present healthy regional character and initiative; in brief, would mean the first step toward the process of substituting the principle of centralism in our new banking system for the principle of regionalism. I value the principle of regionalism so highly that I should look with scepticism on any proposal which would have a tendency to weaken or destroy it. When it is noted that those who wish to widen the base of the reserve note by changing it from a note specifically secured by an equivalent amount of commercial paper to one issued upon the gen-

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eral credit of the Reserve Banks, either have proposed or have in mind as the next step in the development of the new note system, the making of reserve notes legal reserve money for member banks, just as the notes of the Bank of France and the Bank of Germany are reserve money for the banks of those countries, it is clear that the change would be of such far-reaching portent as almost to be subversive.

A freely issued bank-credit note, having the character of legal reserve money for member banks, would involve so considerable a step in the transformation of our new banking system, that I could regard it as nothing less than the disintegration of the system as originally conceived and set into operation. The moment that the note of a Federal Reserve Bank, with the requirement of the minimum gold reserve as the only serious restriction upon its issue, can be counted as reserve by member banks - in other words, from the moment that the constitution of the Federal reserve note is changed from that of a note issued in response to a definite commercial need, evidenced by the fact that the note issued is covered by an equivalent amount of pledged commercial collateral, or in other words, from the moment that a considerable element of discretion and judgment as to the mode of issue enters into the determination of the quantity and therefore of the value of the Federal reserve notes - those notes, if allowed to be counted as reserve money by member banks, must be subject, in the interests of the community's safety, to a degree of centralized control such as would be inconsistent with the spirit and method of

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the regional banking plan. It is unthinkable that twelve banks should be in a position to issue notes which would be available as reserve money - in other words, that there might be twelve varieties of bank reserve money, similar in nothing but appearance and the fact that they bore the indorsement of the United States Government. I am forced to the conclusion, therefore, that the moment that the notes of the Federal Reserve Banks are clothed with the potentiality of bank reserve money, the Reserve System will either be metamorphosed into a central banking system, or something akin to the process of metamorphosis will take place under one form of disguise or another, by the gradual sterilization of the separate Reserve Banks.

The injection into the gold supply question at this time, therefore, of the proposition to change the character of the Federal reserve note implies so much more than it appears to, that it is either to be regarded as academic and gratuitous, or as tending toward a gradual and ultimately a radical reconstruction of the Federal Reserve System, and a perversion of its most fundamental principle. As such, I can not but view it with the most serious apprehension. The regional principle is the vital principle in our new banking system. It is America's specific contribution to the business of reserve banking. A banking system is a growth and development, and the regional principle, which is the life-giving force of the Federal Reserve System, grew out of the clearly perceived necessity of adapting the structure of any system of reserve banking which would fit American conditions

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to the analogies of our political and economic life and the genius of our people. Two years of close and constant contact with the administration of the Federal Reserve Syatem have convinced me of the supreme value and the entire practicability of the regional principle. The wisdom of this foundational feature of the Reserve Act has already been abundantly vindicated. I am sure that we shall prize it the more as we understand it the better, and that we will not, therefore, admit anything that is inconsistent with it or that threatens it.

A.C.M.
10-20-16.

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N O T E

Our country is in a fair way, because of fortune and circumstance, to become an international banker, and either to share the responsibility of international finance with England or possibly to replace England. This circumstance gives an added and more vital importance to the question of the policy that we shall pursue in the matter of our bank note issues. A country that expects or desires to hold a position of prominence in the field of international finance and banking, can not afford to publish to the world or even admit to itself that it is willing to treat as money in its banking reserves anything except what is universally recognized among the trading nations of the world as incontestably money of account. Such has been the policy of England, the only country in the history of modern commerce or since banking has entered upon its modern development that has successfully occupied the position of a world banker. England's financial prestige has long owed much to the unalterable and unassailable determination of her banking leaders to maintain the pound sterling in an impregnable position. The pound sterling in England has always meant a pound sterling in gold. Sterling credits, therefore, always meant gold credits. That is why the English financial community is struggling so hard at the present time to prevent the pound sterling from going the way of the mark and the franc, by maintaining at whatever cost specie payment.

The Bank of England note, issued, as is well known, under

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restrictions which make it so nearly a bullion certificate as to be practically the equivalent of bullion, is, for this very reason, held principally in the vault reserves of the English banks. No fiduciary note, however carefully supervised, would be acceptable in the reserves of the British banker, and it is noteworthy in this connection that, notwithstanding the desperate struggle for national existence in which England is engaged and the necessity under which, in consequence, she finds herself of making her available banking resources reach as far as possible in support of public and private credit, no change has taken place in the status of the Bank of England note nor is such a change in contemplation, because British banking opinion is too alive to the importance of maintaining the structure of commercial and banking credit on a specie basis.

The time was, about 1830, when the restriction upon the Bank of England notes was open to some criticism, as impeding the supply of the country with an elastic currency; but bank notes have long since ceased to supply the currency requirements for business circulation in England as in the United States. Hartley Withers, writing since the beginning of the great war, and reflecting the point of view of the English banking community, says "Now that it is more clearly perceived that the money of England is the check - - - - - - - and that the Bank of England note is chiefly used as part of the bank's cash reserves, the opinion is commonly held in the City that the restrictions on the issue of Bank of England notes should be carried still further, and that that part of the issue which is

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fiduciary or based upon securities should gradually be abolished, the securities behind it being replaced by gold. . . . . As a matter of theory, it is safe to say that a majority of well-informed City opinion is now in favor of making the Bank of England note a pure and simple bullion certificate, and this change of opinion concerning the only law which seriously restricted the banker in the conduct of his business is characteristic of the extent to which English banking has been modified by the development of the use of the check. It has been revolutionized rather than modified, for the check has freed banking. . . . . and at the same time given the commercial community the most perfectly safe, elastic and adaptable form of currency that the world has yet seen". - From Bagehot's "Lombard Street". (Introduction by Hartley Withers, pages ix,x, and xi)

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1572

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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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

October 21, 1916.

Dear Sir :

Please obtain and forward to this office , for the use of the Board in considering applications under the Kern Amendment, maps of all large cities in your district in which an appreciable number of banks and trust companies have interlocking directors. Please indicate on these maps, by numbers , the locations of the respective banks and trust companies, and attach to the maps lists of the names of the banks and trust companies with their corresponding numbers opposite.

The Board would also like to have it appear what institutions interlock either by having this shown on the map, or by a statement on the margin of the same.

Very truly yours,

Governor.

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COPY OF TELEGRAM SENT TO ALL

FEDERAL RESERVE AGENTS

October 23, 1916.

Board is advised that an acceptance credit approximating one hundred million dollars, drawn on American banks and trust companies, is about to be concluded, on ninety day drafts, subject to five renewals, the accepting banks committing themselves to advance the money to the foreign borrowers at five and one-half per cent per annum, plus acceptance commission of one-fourth per cent for each three months. In view of widely circulated press statements that these acceptances will be eligible for rediscount or purchase by Federal reserve banks, Board deems it its duty to point out that banking prudence and obligations toward general commercial interests of the country require that Federal reserve banks should not acquire acceptances of this character beyond a conservative amount. This view is consistent with the Board's policy in the past, and while it wishes, through all legitimate means, to promote the development of the American acceptance market and to further the growth of our export trade, and while it wishes to avoid any attitude of interference with the powers of member banks in this respect, Board feels nevertheless that it should be clearly understood that these acceptances which represent obligations for cash advances aggregating a very large amount, by the acceptors for eighteen months, cannot properly be regarded as paper self-liquidating within a period of ninety days. If offered in excessive amounts, Federal Reserve Banks may be obliged to discriminate against or to exclude entirely acceptances of this character. Board feels that prospective acceptors should have a clear understanding of this.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

October 30, 1916.

S i r :

Inasmuch as the date when the next installment of reserves will be payable by member banks to Federal reserve banks is approaching, the Federal Reserve Board has directed the transmission of this letter for the purpose of securing uniform action with reference to such payments.

Section 19 of the Federal Reserve Act requires each member bank not in a reserve or central reserve city to keep

> "in the Federal reserve bank of its district for a period of twelve months after said date two-twelfths, and for each succeeding six months an additional one-twelfth,"

of 12% of the aggregate amount of its demand deposits, and of 5% of its time deposits. Similar language is used with reference to the banks in reserve cities.

The "said date" referred to is the date officially announced by the Secretary of the Treasury for the establishment of a Federal reserve bank in any district. That date was November 16, 1914.

It therefore follows that on November 16, 1916, country banks and banks in reserve cities will be required to pay their Federal reserve bank an additional installment of reserves. The amount thus to be paid by them will be for country banks one-twelfth of 12 per centum of their demand deposits, as held on and after November 16, plus one-twelfth of 5 per centum of their time deposits; and for banks in reserve cities one-fifteenth of 15 per centum of their demand deposits, plus one-fifteenth of 5 per centum of their time deposits.

It is suggested that each Federal reserve bank call the attention of each member bank to the date upon which the transfer of reserves above referred to is due, and that it arrange such additional details with member banks as may seem desirable. The Board recommends that the member banks be called upon to pay their own express charges, unless there is some good reason why the

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Federal reserve bank of the district thinks it best to bear these express charges itself. The form in which payment is to be made may be suggested by the Federal reserve bank in such circular or notice as it may send out, and it will be well to make some reference to the provision of the Act that any Federal reserve bank may receive from its member banks as reserves not exceeding one-half of each installment eligible paper as described in Section 13, properly endorsed and acceptable to the said reserve bank.

It may also be desirable to call attention to the fact that under the amendment to Section 11 of the Federal Reserve Act approved September 7, 1916, the Federal Reserve Board is authorized to permit member banks to carry in the Federal reserve banks of their respective districts any portion of their reserves now required by Section 19 to be held in their own vaults. The Board, under authority of this amendment, has already issued a ruling to the effect that such member banks may carry all or any part of such reserves in their respective Federal reserve banks.

Very truly yours,

Secretary.

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THE PRESENT POSITION

AND

FUTURE DEVELOPMENT OF THE FEDERAL RESERVE SYSTEM.

****

Address of

W. P. G. HARDING

Governor Federal Reserve Board

before the

FORUM OF THE NEW YORK CHAPTER, AMERICAN

INSTITUTE OF BANKING.

New York, Nov. 1, 1916.

FOR RELEASE THURSDAY MORNING, NOVEMBER 2, 1916.

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THE PRESENT POSITION AND FUTURE DEVELOPMENT OF THE FEDERAL RESERVE SYSTEM.

****

An intelligent treatment of this subject seems to require a brief review of our banking history during the past two years and an analysis of present conditions, out of which reasonable deductions as to the future may be based. The fundamental principle of the Federal Reserve Act is the mobilization, in a scientific and effective manner, of the banking reserves of the country, not in one central reservoir, but in a number of them, distributed throughout the various sections. This process has not yet been fully accomplished, but is approaching completion. The next installment of reserves, which is the last that will be obligatory, and which will amount to about $60,000,000, will be paid in on November 16th. According to the most recent statement, October 28, 1916, the twelve Federal Reserve Banks held $407,955,000 in lawful money, while the national banks of the reserve and central reserve cities, on September 13. 1916, held $515,690,000. These last named institutions held $671,768,000 according to the last statement issued before the organization of the Federal Reserve Banks. There is, of course, no basis for comparison between these figures and those applicable at the present time, owing to the great industrial and financial changes which have taken place during the past two years; and, as bank deposits are

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subject to the influence of external changes of various kinds, it is obvious that any attempt to isolate the effect of the establishment and operation of the Federal Reserve System upon these holdings of cash, would be useless. We can, however, say with certainty, that there is today a co-ordinated and efficient system of reserves available for the ordinary requirements of member banks, as well as for their necessities in times of stress. Three years ago there was a very general fear on the part of bankers that the transfer of reserves would be accompanied with serious inconvenience and loss, and the manifestation of this apprehension is responsible, no doubt, for the gradual rather than immediate transfer of reserves that was provided for in the Federal Reserve Act. The figures already given show, however, that no inconvenience or hardship has been incurred, but that on the contrary, the strength of the member banks and the growth of their deposits and banking power have advanced step by step with the progress and development of the Federal Reserve System. You will note that I have not said <u>because</u> of the Federal Reserve System, although I might perhaps properly have done so. Even the most prejudiced critic must admit the co-ordinated growth of the member banks and of the Federal Reserve Banks, and must concede that the establishment of a great system of mobilized reserves, amounting at present to $407,955,000, the actual and potential value of which is no longer open to doubt, has been effected without even a seeming set-back to the member banks out of whose resources this great reserve has been constructed. The foundation of

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this reserve with its assurance of safety to the banks and to the public, is the first and fundamental achievement of the Federal Reserve System. It is the point of tangency between our new banking system and the well tried systems of other countries, where it has become possible for us to attain the object long ago found desirable and necessary by advanced modern nations, - the establishment of an effective and properly controlled system of credit accommodation, available for the immediate conversion into cash or credit of short time paper of a commercial and liquid character, - in other words, the creation in this country of a broad and dependable discount market.

Closely connected with the foregoing is the provision for an elastic note currency. Through the Federal Reserve Banks there has been provided an adequate method for supplying a circulating medium of exchange based upon commercial transactions in an amount to be determined by the volume of business and by the ability of the banks to supply the requisite gold reserve. There are outstanding $234,876,000 of Federal Reserve notes, to secure which the Federal Reserve Agents hold $219,502,000 in gold certificates and coin, and $15,817,000 in commercial paper. The Federal Reserve Banks themselves hold $407,955,000 in gold and lawful money and $107,216,000 of commercial paper, including rediscounts for member banks and purchases of acceptances on the open market, nearly all of which, under the recent amendment to the Federal Reserve Act, are available for Federal Reserve note issues. The free gold, that is, the amount in excess of reserves against Federal Reserve notes outstanding

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and against deposits held by the Federal Reserve Banks, amounts to $231,377,000, so that the potential note issuing power of all the Federal Reserve Banks, based upon the minimum reserves of 35 and 40% respectively, is today about $578,442,000. This of course, presupposes a demand for the notes which would first be evidenced by the acquisition of commercial paper to a corresponding degree. Of the Federal Reserve notes so far issued, all but $15,374,000 have a full 100% gold cover in the hands of Federal Reserve Agents, so that the comparatively small amount actually outstanding as Federal Reserve notes may properly be regarded as merely an indication of the method through which currency may be obtained when desired from Federal Reserve Banks and is not to be taken as a measure of the relief that may be supplied through this means when the machinery of the System is fully called into play. Experience thus far, limited though it has been, has shown that the machinery for the issue of the notes provided for by the Federal Reserve Banks, can work promptly and effectively, and there is no reason to doubt that whenever it may be called upon to render extended service in times of stress or difficulty it will be able immediately to meet the requirements of those calling for assistance through the medium of note issues.

Although not yet two years old, the Federal Reserve Banks have done much to standardize commercial paper in this country. The circulars and regulations of the Federal Reserve Board have supplied an authoritative definition of commercial paper of various kinds which has been lacking in our banking practice heretofore, while the efforts of the Federal

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Reserve Banks to bring about a larger use of credit statement forms by the member banks, and to secure the co-operation of banks and borrowers in putting their paper into shape to conform to the regulations of the Board, constitute the first organized effort to bring about uniformity of action and practice in the direction desired. That the steps already taken are having an important influence in standardizing methods of accounting and in bringing about a uniform understanding of the meaning of various commercial terms, is not, I think, open to question. Credit must therefore be given to the Federal Reserve System for having taken the first practical step toward bringing about a reform long desired by financial students and by practical business men, - the standardizing of credit methods and commercial paper throughout the United States. The Federal Reserve System has operated also toward stability and uniformity in rates of interest throughout all sections of the country, as is evident at a glance at a table showing the official discount rates in all Federal Reserve districts. To what extent the reduction in discount and interest rates that has taken place during the past two years is due to the establishment of the Federal Reserve Banks, it is, of course, difficult to determine, for the net inflow of gold during that time has amounted to between $600,000,000 and $700,000,000, and this large addition to the basic money of the country has, of course, had a powerful effect upon rates. We have, however, seen low interest rates in by-gone years in certain sections and on certain classes of paper at times when other sections and other borrowers were

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not included in the scope of the interest reduction. It may be claimed with confidence that the Federal Reserve System has operated toward stabilizing interest rates and toward making them more uniform. It is pointed out by economists that the rate of interest is made up of three distinct elements; one providing a return for the labor and amount of investigation involved in analyzing and consummating any particular operation, or the overhead cost; the second is concerned with the remuneration necessary to induce the owners of capital to part with it, while the third is connected with the risk involved and the insurance against the risk. In general, reduction of interest rates through the operation of Federal Reserve Banks is in part a reduction of this last element of cost, - a lowering of the element of risk, as the Federal Reserve System has provided a method for the recognition of unquestionably good paper and for the adjustment of the rate of interest on such paper, so that it will more nearly correspond with the actual value of the funds employed. In other words, methods have been provided whereby legitimate and conservative borrowers all over the country can obtain accommodations at rates approximating a standard on the kind of paper that they have to offer and are relieved of the necessity of paying more in the proportion that they are able to demonstrate their own responsibility and solvency. The advantage of this reduction has been most appreciated by the small business man, who in the past may have been unable to obtain the rate of interest to which the character of his paper, and his own personal standing, efficiency and general condition of

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solvency entitled him. Besides meeting the needs of the general public and of the business community, the Federal Reserve System has rendered also a direct and important service to the banks themselves, not only in making it safer for them to do business, but in actually extending their field of operations and their avenues for profit. Three distinct lines of business are now open to national banks, from which, before the passage of the Federal Reserve Act, they were absolutely barred. As you are well aware, national banks are now permitted to do an acceptance business, making their acceptances either against transactions involving the importation or exportation of goods, or against certain domestic transactions, as provided by the Federal Reserve Act and defined by the regulations of the Board. Then again, wherever not contrary to state law, national banks may, by conforming to certain regulations, exercise fiduciary powers, which functions were formerly forbidden them. Finally, the new law has enabled a large proportion of the national banks to make loans under safe and conservative conditions, upon real estate, - not only upon farms, but also for periods not longer than twelve months, upon other kinds of improved property.

While there are twelve Federal Reserve Banks, each governed by its own board of directors, and each an independent unit, they are all co-ordinated through the Federal Reserve Board, to which body has been given extensive powers of supervision. The banks, though each is independent within its own district, in the general conduct of its business, are the component parts of a great system and the law has provided means for an effective mobilization of the resources of all for the relief of any;

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and, while it has never yet been necessary for one Federal Reserve Bank to call upon another to rediscount paper for it, facilities have been provided and are ready, so that the strength of the entire system is available for the support of any particular district which may at any time experience a demand that would tax its own resources. The fact that no such action has been necessary thus far is strong testimony as to the sound workings and beneficial influence of the system itself, but it is worth while to note that machinery for this kind of relief is always available and in working order. Without attempting any specific enumeration, I will ask you to think of some of the sensational and grave events that have transpired at various times during the past two years, which have threatened crises, not only in our relations with foreign countries, but in our domestic affairs as well. Through it all there has been no disturbance whatever in our money markets; no abnormal fluctuations in discount rates, and no panicky conditions. Do you think that before the establishment of the Federal Reserve System it would have been possible for our financial community to have remained unruffled and serene in the face of such tremendous shocks, or to have undertaken the vast credit operations that have been engaged in so successfully?

The Federal Reserve System is already an important factor in the development of our foreign trade, and is destined to play a much larger part in this particular field. I have already made a brief reference to the acceptance powers of national banks. The acceptance has long been recognized abroad as a most convenient as well as essential piece of machinery in carrying on international transactions, but until recent years

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its use in this country was practically unknown. The national banks and state institutions in some of the states now have the power to accept, so that when we contemplate the future development of the Federal Reserve System, there is hardly any banking function that will play a more important part than the acceptance business.

Figures recently compiled by the Board show that there are now outstanding about $175,000,000 of drafts accepted by American banks and bankers, of which about $100,000,000 have been accepted by New York banks and bankers. These acceptances have found a ready sale at low rates in the open market and about $86,000,000 of them are now held by Federal Reserve Banks, having been taken under regulations issued by the Board, but it must be remembered that the regulations of the Board are necessarily broad in their scope and are not intended to deal with specific cases. They are intended to be permissive within the limitations defined, but the extent to which Federal Reserve Banks should invest in any class of "eligible" paper is a question to be determined as a matter of policy, in accordance with the changing position and requirements of the Federal Reserve System as a whole. While the Federal Reserve Banks have been and doubtless expect to continue to be liberal purchasers of acceptances, the directors of these banks are charged under the law to "administer the affairs of said banks fairly and impartially and without discrimination in favor of or against any member bank or banks, and shall, subject to the provision of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements and accommodations as may be safely and reasonably made, with due regard for

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the claims and demands of other member banks." They must, therefore, in view of possible calls upon them, keep in mind some limitation of their investments in paper which is not in the highest sense self-liquidating or is not of an intrinsically liquid character, however secure and however certain its ultimate payment; and while the member banks have entire freedom of discretion as to transactions in which they may lawfully engage and as to investments which they may legally make, they should not forget that there are certain kinds of paper which will always be preferred by Federal Reserve Banks over other forms of credit, and which can be negotiated at lower rates.

We are no longer a debtor nation. Our current obligations to Europe were liquidated many months ago. We have already absorbed the larger part of the American securities that were held in Europe when the war broke out, and our advances to other countries now exceed $1,900,000,000. Furthermore, our exports to foreign nations are now in so vast a volume as to render full and immediate settlement in gold impossible. We are absorbing every month more than the world's total new production of gold and we are receiving large sums from the hoarded stocks of nations now debtors to us. But even with this, large credits are necessary to sustain our exports. Through force of circumstances the United States is now the world's banker and must continue to act in that capacity for a long time to come, and if we make proper use of our

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opportunities, we can remain permanently, at least as one of the bankers of the world. We must expect to be called upon abroad to render much of the service that has hitherto been performed very largely by England in extending those short term credits which the world requires in the production and transportation of all kinds of goods. The nature of the acceptance business is such that it can best be carried on by those countries that have the lowest discount rates and have the freest and most reliable gold markets. Hitherto the country enjoying these facilities to the greatest degree has been England, and partly for that reason and partly because of her command of the carrying trade, she has been able practically to monopolize the short credits which her bankers had handled through the medium of acceptances. While we have an opportunity now to extend our business with all nations, including particularly those neutrals whose accustomed credit facilities have been cut off or curtailed, the services we render must necessarily redound to our own benefit from a banking standpoint, not only because the extension of proper credits is a sound and profitable business, but also because the establishment of an acceptance market, made up of traders and bankers from all over the world, will bring to us a new element of great strength. The proper financing of our foreign trade ought to prove a most efficient means of protection for us, whenever

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the golden tide now flowing so strongly toward our shores begins to ebb and finally to turn the other way, running out perhaps so fast as to reveal rocks and shoals whose existence we had forgotten. Under such circumstances, by the simple process of raising our discount rate we should be able to force foreign debtors to finance themselves elsewhere and to pay us off. The more the banks begin to participate in the development of the acceptance market, the more they will understand it and the more will grow their habit of purchasing these acceptances, recognizing in such paper the most liquid investment for which a broad and dependable market at minimum rates may always be expected, whether they expect to sell in the open market or to the Federal Reserve Banks. But the most important feature in the successful development of an acceptance market, in fact, a vital principle, must be the intrinsic liquidity of the paper dealt in. It should be plainly understood that an acceptance transaction is essentially a loan of credit rather than of money, and it is of the essence of an acceptance in its true sense that the drawer shall place the funds in the hands of the acceptor on or before the due date of the acceptance, so that the acceptor will not be called upon to use his own funds in paying the maturing obligation. That is an eventuality which should arise only in the case of the drawer's bankruptcy, and against which the acceptor should be well protected by the security taken before the acceptance is made. In the free and

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natural development of a discount market the drawer or endorser of the acceptance should be the one to rediscount the paper or to offer it on the market, and it should not be the acceptor even though possibly there may be exceptional conditions under which the acceptor would be justified in purchasing his own obligation in order to withdraw it from the market. It is not the custom abroad for acceptance houses in the usual course of business, to purchase their own acceptances and to offer them after having once acquired them. In the regular course it is distinctly understood that the accepting firm does not offer on the market for its own account its obligation created by its acceptance, and the practice is quite the contrary. The acceptor may reside in London and the holder by purchase may be in Paris, Berlin, Liverpool or New York, retaining the bill in his possession until it matures. This process up to the present time has not been emphasized in this country, but it is essential for the proper development of the discount market that the business should take this course. We should be careful not to confuse commercial banking with investment banking, nor should we permit our discount market to become so saturated with offerings intrinsically of an investment character, as to influence discount rates and impede its free operation. The Federal Reserve Act distinguishes clearly between these two forms of banking and specifically excludes from purchase or discount "notes, drafts or bills covering merely investments or issued or drawn for the purpose of carrying or trading in stocks, bonds, or other investment

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securities, except bonds or notes of the Government of the United States." The Federal Reserve Act applies particularly to commercial transactions, and lays stress upon the importance of liquidity by stipulating that Federal Reserve Banks must not buy bankers' acceptances having more than ninety days to run, and in its original form it provided that acceptances should be given only in transactions involving the importation or exportation of goods. The recent amendment to the Act has extended the acceptance power so as to apply to transactions growing out of or involving "the domestic shipment of goods, provided shipping documents conveying or securing title are attached at the time of acceptance, or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples." It is clear that the intent of the Act is to safeguard the self-liquidating character of acceptances, as securities of an investment nature are barred, and provision is made that the transaction should be based upon either an actual sale of goods or upon the conveyance of legal title to goods which can be readily marketed so as to protect the acceptor. Quite naturally, under conditions now existing throughout the world, the Board was, soon after the establishment of the Federal Reserve Banks, called upon to consider the question of renewals of acceptance credits. In European countries there are practically no legal restrictions governing the acceptance business, and in order to establish dollar acceptances in competition with sterling bills, or with those drawn in francs or marks,

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the Board ruled that certain renewals of acceptance credits which clearly grew out of the shipment of goods in the first instance, need not, as a matter of principle, be excluded, and Federal Reserve Banks were advised that they might consider as "eligible" bills having not longer than three months to run and drawn under such credit arrangements. The American acceptance is now quite well established in the world's markets, being well known in almost all parts of the globe; and even in those countries which three years ago had a monopoly of the acceptance business, American credit facilities are now being used. Speaking, not so much from the standpoint of the Federal Reserve Banks, but from that of the American banker generally, it would seem proper to extend acceptance credits in liberal amounts to facilitate commercial transactions all over the world, and while we may expect to see this acceptance business grow into very large figures, we must not permit either our ambition, our desire to assist others, or considerations of profit, to run away with us and to cause us to disregard long established and sound banking principles, the observance of which is so necessary for the safety of our Federal Reserve Banking System. There are two rules in this connection which it may be well to emphasize. One is that acceptances should finance the drawer and not the accepting bank. When a banker makes a cash advance at a given rate of interest for a certain length of time, he should not ask his debtor to draw upon him for the purpose of enabling the banker

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to reimburse himself by the sale of his acceptance for the advance which he has made to the debtor. Such a process would make it possible for a long term borrowing to be financed by an accommodation bill drawn for the benefit of the banker. Such a draft would not be essentially self-liquidating. The real borrower may have secured the advance by renewal agreements for eighteen months or two years, at a fixed rate for the entire term and not subject to readjustment at any renewal period. He is not concerned in the discount transaction, and when the first bill matures the advance will continue to run and attempts will be made to rediscount or sell the draft. A bill of this kind is known as a finance draft, and other bills, which also may be called finance drafts, are drawn by brokers or individuals upon a banker and accepted against the deposit of investment credits. Drafts of the description last mentioned may be attractive where the transactions offer handsome profits because of the great difference in interest rates prevailing in two countries and by reason of tempting fluctuations in foreign exchange rates. It is clear that banking prudence requires abundant security in transactions of this kind if they are to be engaged in at all, and that a bill so created has no place in the portfolio of a Federal Reserve Bank. A foreign draft based originally upon importations of goods from this country and drawn upon an American banker with a definite agreement on the part of the domestic banker for several renewals at an interest rate fixed for the entire period covered by the renewals, does not give the chief advantage which should accrue to the banks of a country granting foreign acceptance credits,

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because, no matter to what point the Federal Reserve Banks, if this country be concerned, or the central banks, in case of other nations, might raise the discount rate, it would have no effect upon the foreign debtor, for, having provided at a given rate for his requirements until the expiration of the last renewal, no increase in rates would move him to cover his acceptance and seek accommodation in his own country, because during the term of the extended credit he would have no interest in the discount rate of the country upon which he has drawn. Not the original debtor, but the acceptor would be the borrower in the discount market, and as regards the original borrower, the acceptance would become merely an accommodation draft for the benefit of the acceptor, who alone would be subject to the changing vicissitudes of the discount market. It is equally clear that drafts drawn in one country upon another against long term securities are not self-liquidating, no matter how short a time the drafts themselves may have to run. Where acceptances are based upon actual commercial transactions, the sum total of acceptances bears a definite relation to and is regulated by the volume of international trade, but if bills are accepted against securities, this automatic regulation is lost, and if finance drafts are permitted to be drawn without discrimination, they would continue to pile up just as long as there is a substantial difference in the interest rates of the two countries involved. It is entirely natural and proper that countries or sections where wealth has accumulated and which have large holdings of gold should

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afford credit facilities to their neighbors. As between nations this can be done through short commercial credits by means of bankers' acceptances, where the acceptance is liquidated out of funds coming from the borrower before maturity; or as an investment proposition, by transactions outright in securities issued or held by citizens of the borrowing country. There is no reason why both methods should not be perfectly sound, but the lenders of credit should distinguish clearly between the two transactions. The discount market, which is intended to deal with short term and commercial borrowings, should not be used or abused so as to serve as an adjunct of the investment market. It may not be possible, of course, always to apply these principles with absolute rigidity. We are living in abnormal ti mes and there may be abnormal conditions when temporary exceptions to rules governing normal times may be expected, but such exceptions, whenever permitted, should be kept within reasonable bounds, nor should it be forgotten that they are exceptions and do not constitute the rule. However anxious we may be to continue as a world factor in trade and finance, and however desirous we may be that the wonderful prosperity which we are now enjoying should continue indefinitely, we should remember still that if the time should ever come when our debtors can no longer offer us satisfactory settlements or when our own power of absorption may have reached its limit, that whenever that moment should arrive it would be more satisfactory to contemplate some slowing down of our

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enormous business than to buy its continuance at the expense of undue hazard, and that the loss of interest on idle gold is better than the loss of principal.

In some important particulars the Federal Reserve Act has not thus far been applied at all. The law empowers the Federal Reserve Banks, with the consent of the Federal Reserve Board, to open and maintain banking accounts in foreign countries and to appoint correspondents and establish agencies in such countries for the purpose of purchasing, selling and collecting bills of exchange, and to buy and sell with or without their endorsement, through such correspondents or agencies, bills of exchange arising out of actual commercial transactions having not more than ninety days to run, and which bear the signature of two or more responsible parties. Under conditions that have prevailed since the establishment of the Federal Reserve Banks, it has been thought best to disregard any temptation of profit and to go slowly in entering the foreign field, so that, up to this time the Federal Reserve Banks have no foreign accounts. Upon the close of the war, however, with the United States playing an increasingly important part in the foreign trade and vested with the responsibility of determining the relationship between American and foreign institutions under new and difficult conditions, there will be a large field of important work to be covered by the Federal Reserve System in this connection before the Federal Reserve Banks can be regarded as having fully discharged the duties and responsibilities imposed upon them

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by the Act. How great the importance of this phase of their activity may be, can be judged only by those who have formed an adequate conception of the part that is to be played by this country in international trade after peace has been restored.

The business of the Federal Reserve Banks as fiscal agents for the United States Government is not yet fully developed. So far they are acting in a limited way only as fiscal agents, but in the future financial operations of the United States Government the Federal Reserve System will stand ready to discharge the duty of providing for issues of bonds, arranging for the retirement and refunding of existing indebtedness, and such other financial operations as may be necessary from time to time. Its functions in the handling of routine business for the United States Treasury and the sub-treasuries will no doubt be extended, as the Federal Reserve Banks become better able to render this service.

The clearing of country checks provided for under Section 16 of the Federal Reserve Act, has been a problem of peculiar difficulty and has been complicated by the desire of many of the member banks in the smaller towns particularly, to retain their accustomed profits, and further by the fact rhat a large volume of the checks that must be handled are drawn upon non-member banks. The clearing of checks was undertaken in a very limited way immediately upon the establishment of the Federal Reserve Banks, and after a great deal of study and some experimentation, the present clearing system was put into effect on July 15th last. Its

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operation has demonstrated that it is based upon correct principles, and the constantly expanding volume of business handled through it shows its efficiency. The underlying principle of the clearing plan is the discontinuance of the practice of carrying items in transit as reserve, and the requirement that each bank carry its own float. One important result of the clearing system has been to bring the member banks into more frequent and intimate contact with their Federal Reserve Banks, so that the Reserve Banks are now regarded more and more as active and potential factors in the banking field and not so much as storage reservoirs for use only in emergencies. Very largely, no doubt, because of the abnormally low rates for money that have prevailed during the past eighteen months, which have made it difficult for member banks to make satisfactory earnings, there has been a feeling in some quarters that the Federal Reserve Banks are dangerous competitors, actual or potential, of their own member banks, but with the development of our foreign trade and with the constantly increasing activity of our domestic business, this feeling is gradually passing. The managements of the various Federal Reserve Banks and the members of the Federal Reserve Board, with an appreciation of the value of thorough co-operation and complete understanding, have kept in close touch, both by correspondence and by frequent personal contact, so that the Board has been kept informed of local conditions and the Federal Reserve Banks are made familiar with the viewpoint of the Board on matters of policy. Just as this co-operation and understanding

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between the Board and the banks is necessary for the best development of the Federal Reserve System, so is it essential that there should be the same close relationship between each Federal Reserve Bank and its own member banks. The scope of the Federal Reserve Banks and the activities in which they may properly engage, and the functions which they were created to discharge, are all being better known as time passes. Some who, at the beginning, were its severest critics, are now among the strongest advocates of the system. There are few today who would wish to wipe it out or to reconstruct it radically, and when again conditions throughout the world approach the normal, it will be the most powerful agency in assuring to the United States a sound financial position at home, and in securing for our country its proper place in the realm of world finance.

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

W A S H I N G T O N

October 27, 1916.

SUBJECT: Acceptances of Member Banks.

My dear Governor:

Section 13 of the Federal Reserve Act, as amended by the Act of September 7, 1916, vests in member banks the power to accept drafts or bills of exchange in certain specified transactions. This Section reads in part as follows:

> "Any member bank may accept drafts or bills of exchange drawn upon it having not more than six months' sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples."

A number of member banks have submitted questions for the Board's consideration in reference to the circumstances under which these acceptances may be made. Briefly summarized the questions submitted are as follows:

(1) Does Section 5202, Revised Statutes, which limits the liabilities that may be incurred by national banking associations, apply to acceptances made by member banks under authority of Section 13 of the Federal Reserve Act?

(2) May a member bank purchase and hold its own ac-

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ceptances carrying them as newly acquired assets of the bank?

(3) Are acceptances of member banks, made under authority of Section 13, subject to the limitations imposed by Section 5200, Revised Statutes, which limits the amount that any person, firm, or corporation may borrow from a national bank?

(4) If a member bank has the right to purchase and hold its own acceptances, are such acceptances, when purchased, subject to the limitations imposed by Section 5200 above referred to?

In order to answer these questions it is necessary to consider the nature of the obligation assumed by a member bank when it accepts a draft or bill of exchange drawn against it and the purpose of that part of Section 13 which adds this new power to those heretofore vested in national banks.

Under the Negotiable Instruments Law and the decisions of the courts, a bank accepting a draft or bill of exchange enters into a contract substantially similar to that of the maker of a note. An acceptance is defined by Norton on Bills and Notes (Fourth Ed. p. 116) as "an undertaking by the drawee to pay the bill when due".

The maker of a note assumes a similar obligation, so that while the form of the instrument differs the legal effect is the same.

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The use of a bank's acceptance, however, differs from the use of its promissory note. A bank desiring to borrow money will ordinarily execute its promissory note or bill payable and discount this note with another bank, receiving the proceeds in cash or in the form of a credit balance. Where a bank accepts a draft or bill of exchange for one of its customers, however, it merely lends its credit responsibility to its customer in order that he may procure the funds elsewhere.

The holder of a bank's acceptance has the same legal rights against the bank as the holder of a bank's promissory note or bill payable, but banks are not authorized by Section 13 to use their acceptance power for the purpose of borrowing money for their own use. They are specifically limited by the terms of the Act to the acceptance of drafts or bills of exchange -

> "(a) Which grow out of transactions involving the importation or exportation of goods;
> "(b) Which grow out of transactions involving the domestic shipment of goods;
> "(c) Which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples;
> "(d) Which are drawn upon it * * * by banks or bankers in foreign countries * * * for the purpose of furnishing dollar exchange, as required by the usages of trade in the respective countries."

The use of the bank's acceptance is limited to the foregoing purposes which are expressly enumerated in the Act and where it appears that this form of obligation is used for unauthorized purposes, or for the purpose of evading restric-

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tions imposed by statute upon the exercise of other banking powers, the substance of the transaction engaged in rather than the form of the obligation assumed should be considered in determining whether such other statutory limitations are applicable.

Considering the foregoing questions in the order in which they appear -

1. Does Section 5202, Revised Statutes, which limits the liabilities that may be incurred by national banking associations, apply to acceptances made by member banks under authority of Section 13 of the Federal Reserve Act?

Section 5202, Revised Statutes, as amended by the Federal Reserve Act, provides that:

> "No national banking association shall at any time be indebted, or in any way liable, to an amount exceeding the amount of its capital stock at such time actually paid-in and remaining undiminished by losses or otherwise, except on account of demands of the nature following:
>
> "First. Notes of circulation.
> "Second. Moneys deposited with or collected by the association.
> "Third. Bills of exchange or drafts drawn against money actually on deposit to the credit of the association.
> "Fourth. Liabilities to the stockholders of the association for dividends and reserve profits.
> "Fifth. Liabilities incurred under the provisions of the Federal Reserve Act."

If, therefore, a member bank assumes the liability of an acceptor in any of the transactions authorized by the Federal Reserve Act, as amended, such liability is expressly exempt

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from the limitations imposed by Section 5202 above referred to by the fifth exception to this Section, namely, "Liabilities incurred under the provisions of the Federal Reserve Act".

Under authority of Section 13 of the Federal Reserve Act, therefore, a member bank may incur authorized acceptance liabilities to an amount equal to one-half of its paid-up and unimpaired capital stock and surplus in addition to those liabilities which are limited by Section 5202 to one hundred per cent of its capital and surplus.

2. May a member bank purchase and hold its own acceptances, carrying them as newly acquired assets of the bank?

In order to answer this question it is necessary to determine the legal effect of such a purchase, that is to say, whether or not the purchase of a bill by the acceptor before maturity, extinguishes the debt and releases the drawer and endorsers. When a bill is paid before maturity by the drawer or indorser there is no question but that the payer may reissue and further negotiate it.

French v. Jarvis, 29 Conn. 347;
Palmer v. Gardiner, 7 Ill. 143;
West Boston Savings Bank v. Thompson, 124 Mass. 506;
Am. & Eng. Enc. of Law, 2d Ed., Vol. 4, page 500.

While the authorities are not entirely agreed in the case of a payment before maturity by the acceptor, the weight of authority seems to be that such a payment operates as a mere purchase of the bill and not a payment of the debt, and that the acceptor may in such case properly reissue the instrument before maturity. The transferee may recover on it against all parties as a bona fide holder for value.

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Morley v. Culverwell, 7 M. & W. 174;
Rogers v. Gallagher, 49 Ill. 182;
Eckert v. Cameron, 43 Pa. St. 120;
Am. & Eng. Enc. of Law, Vol. 4, 2d Ed., p. 501.

In such a case the parties to the instrument are bound as though it had not passed through the hands of the acceptor.

Rogers v. Gallagher, 49 Ill. 182.

A few jurisdictions hold that the payment by the acceptor before maturity extinguishes the instrument, and that a subsequent transferee cannot hold the other parties liable.

Beebe v. Real Estate Bank, 4 Ark., 546;
Long v. Cynthiana Bank, 1 Litt (Ky) 29;

The purchasing bank, however, does not acquire any new or additional assets by this transaction. It uses its cash resources to purchase its own obligation thus reducing its assets and its outstanding liabilities by the amount of the acceptance purchased.

It is assumed that when the draft or bill of exchange was accepted the customer procuring the acceptance entered into a collateral contract with the bank to place it in funds by or before maturity to pay the acceptance when due. As a result of this transaction the acceptance of the bank would constitute a liability and it would have as an offsetting asset the liability or guaranty of the customer. When the bank anticipates payment of or purchases its acceptance it reduces its outstanding liabilities and reduces its cash resources by a corresponding amount, but retains its rights against the customer as one of its assets.

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If it should be claimed that since the bank has the right to reissue or to sell this acceptance at any time before maturity, it should continue to show it as an outstanding liability, it would of course be necessary for it to show the acceptance itself as an offsetting asset in order to balance its books.

The better practice, however, would seem to be to treat the liability as acceptor as discharged and not to show the acceptance purchased as an additional asset.

3. Are acceptances of member banks, made under authority of Section 13, subject to the limitations imposed by Section 5200, Revised Statutes, which limits the amount that any person, firm, or corporation may borrow from a national bank?

From the foregoing it seems clear that if a member bank merely contracts to pay an obligation at maturity by accepting a draft or bill of exchange drawn against it and this acceptance is discounted with a third party, the customer procuring the acceptance cannot be said to have borrowed money from the accepting bank but has merely borrowed its credit, and such an acceptance should not be treated as a liability for money borrowed from such bank within the meaning of Section 5200.

4. If a member bank has the right to purchase and hold its own acceptances, are such acceptances, when purchased, subject to the limitations imposed by Section 5200 above referred to?

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When a bank purchases its own acceptance, however, it has ceased to lend merely its credit responsibility, and has utilized its own funds in purchasing the rights of the holder of the acceptance.

As holder it would have recourse only on the collateral contract for reimbursement against the customer for whom the acceptance was made, and not against the other parties to the bill since the bank as the acceptor is the party primarily liable. Even though the bill were secured by shipping documents, warehouse or trust receipts, this security could be realized on only in the event that the customer defaulted in his contract to furnish funds to pay the acceptance at maturity. Accordingly, when the bank purchases its own acceptance it uses its funds to anticipate the payment of a liability which its customer has agreed to pay at a later date, and in effect makes a loan of its funds to such customer. The evidence of the debt thus created is the customer's contract to place the bank in funds to pay the acceptance when it matures or to repay the advance or loan made by the bank when it purchased the acceptance. The liability of the customer under such circumstances should be treated as subject to the limitations of Section 5200 which provides in part that:

> "The total liabilities to any association, of any person, or of any company, corporation, or firm, for money borrowed * * * shall at no time exceed one-tenth part of the amount of the capital stock of the association actually paid in and unimpaired and one-tenth part of its unimpaired surplus."

The same result would be reached if the accepting bank was called upon to pay the acceptance atmaturity and the customer

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who procured the acceptance had not furnished to the bank the necessary funds to pay it. In either case the liability of the customer would be subject to the limitations of Section 5200. It necessarily follows that where a bank accepts a draft or bill of exchange for one of its customers and immediately discounts such acceptance for the customer, the transaction constitutes merely a subterfuge for permitting the customer to borrow money from the bank. Acceptances discounted in this manner should be treated as money loaned to the customer subject to the limitations imposed by Section 5200 above referred to.

DISCOUNT OF ACCEPTANCES

The purchase or discount of a bank's own acceptance should not be confused with the purchase or discount of acceptances of third parties.

From some of the inquiries submitted there appears to be a tendency to confuse the acceptance power of a member bank with the power of member banks to discount acceptances and it, therefore, seems advisable to consider in this opinion the question of whether or not bills of exchange and acceptances discounted by a member bank are subject to the limitations of Section 5200 above referred to.

It should be remembered that national banks have had the power to discount bills of exchange and acceptances of third parties ever since the national banking system was created in 1864. The right to lend their credit by assuming the obligation

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of an acceptor, however, was not authorized until the passage of the Federal Reserve Act on December 23, 1913. According to the original provisions of this Act this power was limited to the acceptance of drafts or bills of exchange which grew out of transactions involving the importation or exportation of goods.

By the Act of September 7, 1916, it was extended to include acceptances in certain domestic transactions and those made for the purpose of creating dollar exchange. The exercise of this power, however, is in no sense the same as the exercise of the power heretofore vested in member banks to discount bills of exchange and acceptances.

In determining whether the limitations of Section 5200 apply to the discount of bills of exchange or acceptances it is necessary to consider the circumstances in each transaction. Section 5200 excepts from its limitations "the discount of bills of exchange drawn in good faith against actually existing value, and the discount of commercial or business paper actually owned by the person negotiating the same." It is clear, therefore, that a bill secured by shipping documents, or by the pledge of goods actually sold, might be discounted by a member bank before acceptance without being subject to the limitations imposed by Section 5200 since this would constitute a bill drawn in good faith against actually existing value. When such bill has been accepted by the drawee, and the documents attached have been removed, though the direct obligation of the drawee to pay such bill at maturity is substituted for the "actual value" against

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which the bill was originally drawn, nevertheless, when discounted by a bona fide owner for value, its discount would not be subject to the limitations of Section 5200, because it would be "commercial or business paper actually owned by the person negotiating the same."

Should the drawee who accepts the bill, however, attempt to discount it with a member bank it would be subject to the limitations of Section 5200 since in that case the party primarily liable would in effect borrow money from the bank on his own obligation and while such an acceptance might be in the form of commercial or business paper it could not be said to be "actually owned by the person negotiating it." In other words, a bill or an acceptance when offered for discount to a member bank must be in fact as well as in form what it purports or is represented to be, if it is to be treated as coming within the exceptions to Section 5200.

For example, a bill secured by warehouse receipts and drawn by the owner of the goods against himself or his agent or against a fictitious drawee for the purpose of borrowing money would not be a bill drawn in good faith within the meaning of Section 5200. An accommodation acceptance not growing out of a commercial transaction and not representing any debt actually due from the drawee to the drawer of the bill, but drawn solely for the purpose of enabling one of the parties to the bill to borrow money from the member bank, would not be "commercial or business

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paper actually owned by the person negotiating it." Where, however, the bill is drawn in good faith against actually existing value, or where the person discounting the commercial paper is the actual owner of the debt represented by the acceptance, it would come within the exceptions to Section 5200.

Respectfully,

M. C. ELLIOTT
Counsel.

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

11/1/16

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Washington, D. C.,

November 10, 1916.

My dear Dr. Miller:

You were good enough to send me on October 23rd a copy of your Indianapolis speech and an appendix containing some thoughts of yours which you did not think it opportune publicly to express at this time but which you submitted to the Board members for the purpose of bringing about a general crystallization of views concerning this most important topic of note issue and reserves.

In going to the great trouble of reducing to writing our thoughts upon this subject, even though we disagree - or possibly because we disagree on certain points - you and I are rendering a valuable service, for, as you correctly say, the time has come when, after an existence of more than two years, the Board has to take a definite position upon problems which are of so vital a nature and concerning which our banks are now entitled to definite guidance and instruction, one way or the other.

It is for this reason, and not for the pleasure of a controversy, that I think it my duty to analyze your speech and point out, with brutal frankness, where you

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and I are not in accord. The members of the Board, I believe, want to have both sides of the case presented as fully as possible before finally making up their minds.

Before taking up your argument, let me compliment you upon the admirable way in which you have presented it. While I differ from you as to some of your conclusions, I certainly could find no fault as to the form. You made a splendid presentation and you will have to bear with me if I do not attempt to equal your paper as to polish and style. But time is pressing and I shall confine myself simply to enumerating and discussing the various objections as they occur to me.

You are in accord with me as to the main objective of my recent address - that it is our duty to prepare our banking system so as to enable us to withstand large withdrawals of gold.

Let me say right here that I do not consider myself qualified to act as a prophet. I do not know whether at the end of the war gold will be withdrawn at all. Nobody can say that today, because it will depend upon the question whether or not the credit of the now-belligerent countries at that time will still be strong enough to draw gold; and that, again, will depend upon the further duration of the war. On the other hand, it may be that we shall have to lose a great deal of gold. My conten-

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tion is, not that we shall or shall not lose gold, but that it is the duty of a Federal reserve system to forearm in a manner that will enable us to lose gold without creating unnecessary convulsions. That we can protect ourselves and stop gold withdrawls in case they should work havoc with us, I have no doubts. But what I wish to avoid is that we should be forced to do so unnecessarily early, because it would mean that, to our own detriment, we should have to force up our own money rates and that we should have to stop granting credit facilities to other countries. I believe, however, that, having grabbed so large a share of the world's gold and wealth, we should consider it our moral duty to stand prepared to open our doors wide and contribute a phenomenal share in the work of reconstruction and construction that will have to be done after the end of the war.

I have, therefore, little sympathy with your argument that if we prepare to lose about $600,000,000 of gold that we have done our duty. If we should have to lose those $600,000,000 - (the arbitrary amount which you take as the basis of your argument because it happens to be the net accretion of gold at this time, though in a few months it may amount to much more) - our gold reserve on the basis of your calculation would have shrunk to 35 or 40%, respectively. You and I are

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in complete accord that that reserve is the minimum; but a minimum which should not be reached and which could not be considered satisfactory or a safe basis for our banking structure. If we reached that point we should certainly have to stop granting any further facilities outside of the United States, contract credits at home, and try by all possible means to re-establish a higher and safer basis of note and deposit gold cover.

My contention has been that we should be prepared to lose $500,000,000 or $600,000,000 of gold and still have $200,000,000 or $300,000,000 "free gold" in reserve, so as to keep intact our own credit machinery in case these gold exports should occur in these large proportions.

Your point of view is that it is safe enough to begin to hustle to secure these missing two or three hundred million dollars of gold when the emergency arises.

My experience as a banker makes me distinctly disinclined to rely upon that course. I believe that Governor Strong in his letter to you has admirably shown how little reliance in this connection we could place upon voluntary cooperation of our thirty thousand banks. When our reserves are down to 35% they will not be so eager to give us their gold in exchange for Federal reserve notes,

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particularly in times when gold is the one thing that other countries will draw from us and that we, at such time, will not be eager to part with.

And again, if you have in mind a situation such as that at the beginning of this war, you will observe that critical times - particularly during complications that spring up suddenly - bring about increased demand for currency. During those times the banks pay out a lot, but the volume of currency that is paid into the banks and for which alone gold circulation at that time could be substituted, is very unimportant, if at all existent. You have, of course, in mind the illustration of the issue of $470,000,000 additional currency in 1914. If during a critical period a determined appeal should be made to the public to turn in its gold, it might lead to increased alarm and panic, unless we were involved in a situation similar to that governing France and Germany where they were dealing with a national emergency and plainly appealing to the patriotism of all citizens.

But frankly I cannot quite understand why you should have taken exception at all to my point of view. When you figure out why we are strong enough to meet emergencies you rely on three items: One, our actual gold reserve taken

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from the member banks' deposits; two, the amount now impounded with the Federal Reserve Agent; and, three, the increased balances to be kept with Federal Reserve Banks produced by transferring member bank vault money to such Federal Reserve Banks.

As to the process under No. 2, in trying to prove that we are strong enough at this time you base your argument upon $120,000,000 of free gold which the member banks may rely upon, owing to the fact that they have impounded more than $200,000,000 of gold with Federal Reserve Agents. You recognize this method as necessary and advisable in its present scope. You do not object to its being continued as, as a matter of fact, it has got to be, provided the present indirect methods are applied. You also approve that this method of exchanging Federal reserve circulation for gold circulation be fully legitimized and pushed as far as it can be in case your $600,000,000 should prove an insufficient reserve, hence, as a matter of fact, you have sanctioned the process in the past; you sanction it in the present and you rely upon it for the future. And I am frank to say that I do not quite see why you should consider my plan as a process of "artificial shifts and manipulations" "distorting and disfiguring our banking sys-

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tem to its own prejudice and to the prejudice of the country's real interests". As a matter of fact, you approve of the principle and disagree only as to the question of degree, taking it upon yourself to say that a definite amount is sufficient at this time while in other parts of your speech you say yourself that "it will be prudent, in making our calculations, to take note of the possibilities as well as the probabilities, particularly as the latter are so incalculable". However, I would be quite willing to leave your contentions unchallenged and allow nature to take its course if I were not so fully convinced that your process under No. 3 would be practically nullified by your disinclination to legitimize fully and modernize the issue and use of Federal Reserve notes. Practical experience will show you very promptly that, no matter how hard we may try to have our member banks increase their balances with Federal Reserve Banks by transferring a substantial share of their vault money, this will not be accomplished until they may count a reasonable amount of Federal Reserve notes as reserve. Our present deposit structure of member banks is too gigantic to make them either willing or feel justified in operating with a supply of till money which would merely respond to their average till requirements. Every conservative bank

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must be in a position to pay out promptly, without the least bit of hesitation, a very substantial portion of its deposits. They will, therefore, wish to have at their immediate command, without any possible delay, a substantial amount of currency. No doubt they would be willing to rely upon Federal Reserve notes for satisfying their depositors and would be quite willing to keep in their vaults, let us say, an amount equal to about 3% of their deposits. But they cannot afford to do this, because their sending of the corresponding 3% of their gold to the Federal Reserve Bank as additional balance would mean that they would carry, not 3%, but 6% in order to provide this amount of available currency in Federal Reserve notes. That is something the banks will never do. It is a loss which would appear to them entirely unnecessary and unwarranted, and would simply mean that that amount of gold will be kept in their vaults.

You will answer that this may be correct so far as the banks are concerned which are not located in Federal Reserve cities and that banks that are in Federal Reserve cities would afford to rely upon their ability to send across the street to their Federal Reserve Bank and get currency, and that, therefore, these member banks could reduce their cash holdings to the amount which is actually required

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for daily till uses. That would be correct, but it will not work out that way in practice. As a matter of fact, experience shows that the strong banks in London, Paris and Berlin keep a large amount of till money in order to be prepared immediately to meet all emergencies without being forced to send outside of their building, and it also must be borne in mind that these very strong institutions have a sort of pride in not applying too frequently to the central banks. Normally, they like to keep their investments and collections so well balanced that additional cash requirements can be taken care of by collecting a larger proportion of their daily maturities. In our case, that would mean that while the strong member banks may keep large excess balances they will keep part of this excess in their own vaults. Or, if their excess balance with the Federal Reserve Bank is being drawn down or withdrawn, their excess vault money acts as a supplement to their Federal Reserve Bank balance. If in that case they had Federal Reserve notes in reserve it would be necessary for them to send them over to the Federal Reserve Bank and convert them into a balance because otherwise these notes would be useless as reserve, and, under the circumstances, it stands to reason that they will rather hold on to a comfortable amount of gold or gold

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certificates. But there is another reason for their doing so, and that is that as long as the law makes this differentiation between Government obligations, calling the gold certificate, the silver certificate and the greenback first class money and the Federal Reserve note second class money, the member banks will feel a greater degree of safety in commanding the first class money then the second class. The sifting process will, therefore, continue and the large banks will have some kind of a subconscious feeling that as long as the Federal Reserve Banks are paying in currency that is second class and not worth to the member banks as much as what they would consider real first class money that the Federal Reserve Bank balance too is not quite as good as their gold. Moreover, these strong banks, on which a great many correspondent banks still rely, and which are by law obligated to keep the higher reserve of 18% for the very reason that, to a large extent, they are the correspondents of banks, would have a feeling of apprehension lest <u>their</u> gold placed in the Federal Reserve Banks would be used for the protection or credit expansion of the entire country, so that their actual gold reserve would be watered while the thousands of country banks would hold on to their gold. In other words, it

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would be a one-sided proposition which would not appeal to the banks in the Federal Reserve cities and would militate against the carrying out of your plan. This is a most important feature which you must not overlook. It will prove to make your entire program illusory.

But, even if your program could be carried out on the very basis that you appear to have in mind, I would personally consider it a very unfortunate one. The policy of the entire Federal Reserve System in that case could be controlled by the strong banks in the central reserve cities. If at any time the Federa; Reserve Bank became aggressive in a way that would annoy them they could at once collectively reduce the operating power of the Federal Reserve Banks by withdrawing their excess balances and putting them back into their own vaults.

My plan of securing an overwhelming amount of gold for the Federal Reserve Banks by withdrawing it from circulation and making every citizen of the United States who carries a note in his pocket permanently a would-be depositor of the Federal Reserve Bank, would free the Federal Reserve Banks from the exclusive control of their large member banks. Incidentally, as I have tried to show in my previous paper, it would immensely strengthen the power of our system and the confidence that it would command, not only at home, but also abroad.

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You appear to think that the process proposed by me would lead to a "distortion of our gold standard". Nothing could be more unwarranted than such a thought. In my previous paper, I tried to show as plainly as I could that we must differentiate between reserves of member banks and reserves of central banks. Unfortunately, this point of view has been completely left out of consideration in your paper.

The gold standard is not affected at all by what I propose to do. Quite the contrary, my plan has for its very object to mass under our control the gold running wild in our country so that we may better protect our gold standard. If your plan could be carried out, there would remain in the vaults of the member banks only 2% in till money and all the rest would go into the Federal Reserve Banks. This 2% would amount to about $175,000,000. I fail to see why $175,000,000 of Federal Reserve notes placed in the vaults of member banks and against which a minimum of $70,000,000 of gold must be held with Federal Reserve Banks, permitting a net possible inflation of $250,000,000, should frighten you so and justify you in trying to combat a development - which otherwise can only redound to the greatest benefit of the entire country and

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and would, as a matter of fact, secure the independence and growth of the Federal Reserve System - if, on the other hand, you are quite willing to let the total reserve required of about $1,375,000,000 be carried as balances with the Federal Reserve Banks upon which theoretically they could build an additional note issue of about two billions. But we need not be afraid of securing that much. We shall neither get all the gold held in member banks' vaults, nor more than a substantial percentage of the gold now in circulation; but, without the proper recognition of the Federal Reserve note, we will not begin to secure a sufficient supply of gold to provide for adequate strength and growth considering our possible necessities and probable opportunities.

You have in your mind a very distinct apprehension that through the amendment that we have often discussed the character of the Federal reserve note might be destroyed; that we might interfere with "the unique excellence of the note provisions of the Federal Reserve Act which provide a maximum of elasticity with a minimum of danger of over-issue". I give you below a condensed statement of all Federal Reserve Banks as of last Saturday; and underneath you will find the same condensed statement as it would look if our amendment had gone through:

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(I)

FEDERAL RESERVE BANKS
(in million dollars)

Assets:		Liabilities:		
Gold	432	Capital	56	
Paper	110	Govt. & member deposits	580	
Other investments	108	Federal Reserve notes	14	
	650		650	Res. 72.8 Dep.& note

Federal Reserve Agent:

Gold	214
Commercial Paper	14
	228

(II)

Assets:		Liabilities:		
Gold	646	Capital	56	
Paper	110	Deposits	580	
Other investments	108	Notes	228	
	864		864	Res. 77.4 Dep.& note

Federal Reserve Agent:

Collateral :	(Gold	214
	(Comm'l paper.	14
		228

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I wish you would show me how there would be any quicker redemption under (I) than there would be under (II). In effect they are absolutely alike. No matter how we keep our books, there are in effect in both cases $244,000,000 Federal reserve notes outstanding, of which $230,000,000 are secured by gold and $14,000,000 by commercial paper. If this paper is collected at maturity the entire $244,000,000 will be covered by gold. If any Federal reserve notes are actually presented for redemption, nobody could tell whether the originally gold secured notes or the paper-secured notes are paid for. The individual outstanding notes today have no ear-marked collateral of paper or gold. They are in effect secured by both; and all our amendment proposed was a clarification of a condition which, as a matter of fact, exists already today.

Elasticity is a question not of the individual notes but of the aggregate volume of outstanding notes and (the simple substitution of Federal Reserve notes for gold circulation leaving the volume unchanged) this volume is controlled by the increase or decrease of the Federal Reserve Banks' investments. No matter whether or not a Federal Reserve note is held in a member bank's vaults as reserve or is circulating in the pockets of the people, it will be re-

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deemed and converted into gold whenever the Federal Reserve Banks collect their investments. I cannot for the life of me see how the redemption of Federal Reserve notes takes place faster in one case than in the other. It follows automatically the collection of the Federal Reserve Bank's investments.

You say:

> "It is unthinkable that twelve banks should be in a position to issue notes which would be available as reserve money - in other words, that there might be twelve varieties of bank reserve money, similar in nothing but appearance and the fact that they bore the indorsement of the United States Government."

I had hoped very much that you could follow the reasoning contained in my Kansas City speech that, in dealing with member banks, we should stop talking of reserve money, which indeed is an "obsolete" manner which is not even found in England, which you have chosen as your model. Bank balances and vault money are carried there indiscriminately in one item. Whatever is good enough for the public to accept as current money is included in the item "Cash and bank balance" by English banks, and, for that matter, by French, German and other banks. When the Peel Act was suspended in England and notes were issued by the Bank of England against any kind of security there was not a bank in England that would not include Bank of England notes in the item "Cash and balance with the Bank of Eng-

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land". One note of the Bank of England was treated like any other note of that bank. There was no differentiation between those issued against gold and those issued against securities. As a matter of fact, there always has been a certain amount of government securities against Bank of England notes and that never has prevented the English banks from counting those notes as cash. Today, when there are outstanding £650,000,000 of currency notes issued by the British Government, with a gold cover of 21.6%, these currency notes are included in "Cash and balance with the Bank of England" together with Bank of England notes, even though these currency notes are secured by only so small an amount of gold cover and the remaining cover consists of government securities, while our Federal Reserve notes are secured at present by about 100% of gold. No matter what Hartley Withers may say about the desirability or probability of making the Bank of England note a pure gold note at the end of the war, I believe that nothing of the kind will happen and that, quite the contrary, as the probable development we may much rather expect at the end of this war that the Bank of England will be reformed to correspond more to the continental systems with an elastic note issue. Sir Edward Holden's speech on this point is very instructive. As a matter of fact, he had worked out a plan for the English member banks to assemble additional

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gold reserves (for the very reason that the Bank of England, under its present organization, is not able to control a sufficient amount of gold) and, in time of emergency, to deposit this additional gold with the Bank of England and make it the basis of an elastic note issue on the continental plan. Whenever this plan were carried out, the Bank of England notes would be part and parcel of the item "Cash and balance with the Bank of England."

I fail to see any sound reasoning in Hartley Withers' contention. When the bulk of the British banks' "reserves" consist of balances with the Bank of England, which are never fully secured by gold (at present they have a reserve of about 23%), why should the Bank of England note not be included in "Cash and balance with the Bank of England" unless it were secured by 100% gold - which it never was?

But, to return to your argument: If you object to 12 varieties of reserve money, how can you justify that the total reserve of a member bank may be kept as balance with one of the 12 Federal Reserve Banks - balances which in that case are not guaranteed by the United States? Are these not 12 different varieties of reserve money, much poorer protected reserve money at that than the obligation of the United States! Moreover, are you quite justified

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in saying that these notes are

> "similar in bothing but appearance and the fact that they bore the indorsement of the United States Government"?

Is it not a fact that these notes are absolutely identical all over the country except that there has been printed upon them the seal of the respective Federal Reserve Banks to make them distinct as to the point of redemption? In the pockets of the people they are absolutely the same identical instrument. The only difference is that when they come back to the issuing Federal Reserve Bank it may not pay them out. They are not <u>indorsed</u> by the United States. They are the <u>obligation</u> of the United States, and, furthermore, they are alike in this, that there must be held against all of them at least 40% of gold. As far as the member banks are concerned, all these notes are alike. They can present them for payment wherever they please and whenever they hold them they hold the sacred obligation of the United States to pay in gold.

Your paper proceeds on the theory that the Federal Reserve System has been fashioned upon the British as against the Continental systems; that the British system is good and ought to be imitated by us; that the Continental systems are bad, or anyhow that they would be bad models for our Federal Reserve System.

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I have to take issue with both of these points. The most characteristic difference between the Bank of England and other central banks is that the Continental banks have an elastic note issuing power while the note issuing power of the Bank of England is rigid. The very object of the Federal Reserve Act was to provide for an elastic note issue and this note issue was copied from the Continental banks. We had a rigid note issue before the enactment of the Federal Reserve Act and were subject to all its fatal consequences. Are you not blowing hot and cold? On the one hand you consider the Federal Reserve System, with its elastic note issue, a great advance made by the United States, and correctly so. On the other hand, when conclusions are to be drawn, and when we ought to benefit from the experiences of the very countries which developed this method of the elastic note issue, you cling to the principles and the experiences - and bad experiences at that - of the rigid note issue country and, in doing that, you can only create an unfortunate confusion.

I do not want to go too closely into your paper, but it appears to me that the parallel between England and the United States is poorly chosen for the additional reason

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that, while you say the bank note has become obsolete in England, you cannot possibly say the bank note has become obsolete in the United States, where there is a per capita amount of $42 of money. It is not a question of whether or not the bank note becomes obsolete, but it is the question, whether or not the use of money becomes obsolete. If I understand you correctly, what you mean is that in England so much is being paid by check that the actual use of money has become an unimportant feature, and the check has taken its place. But that certainly cannot be said of us. No doubt the check plays a large part but, in spite of that, we have a large volume of money in circulation and a large fluctuation in the volume of money caused by such processes as crop movements, which do not affect England. Moreover, I think you under-estimate on the other hand the amount to which clearings and giro are used on the Continent, tending to reduce the use of actual money. You will find attached a statement of the amounts of obligations that have been settled in Germany either by the giro system or by clearings or by postoffice transfers or postoffice checks. Moreover, as you know, there is a movement afoot in Germany to encourage the use of checks, a

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process which has been started on several occasions but which unfortunately, by reason of a petty fiscal policy of putting a stamp tax on checks, was killed upon each occasion. I mention this only for the purpose of adding that even after the check system is established in France and Germany you will find that there will not be any difference in their method of handling notes. The notes of the Banque de France and the Reichsbank will continue to be counted as cash together with the balance with the central banks.

I should be very much mistaken if, after the war, there would not be a strong development in all now belligerent countries to use the check and to use the bank note as the means of payment of internal debts. The check and the bank note will both act as "yard sticks" and as media of clearing; the gold will be concentrated in the central banks in order to be available for the settlement of international debts.

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I think, dear Doctor, you are moving between two extremes. On the one hand, you are a passionate advocate of the highest development of the use of checks. You have sometimes gone so far as to call the check a "means of currency." On the other hand, however, you appear to me to be an advocate, not of the bank note, but of the gold certificate or actual gold circulation. While I am in full accord with you as to the desirability of the development of the check system, I am distinctly opposed to the wasteful method of using the gold itself as a means of exchange; that is to say, actual barter in each case, actual value, instead of using the "yard stick", the check or the bank note which are obligations to pay in actual money.

I know that you and I are in accord that at this time, when we have grown so tremendously rich and strong through the misfortune of others, it would be nothing less than a crime to build around the United States a high tariff wall so that we may hold all we have taken and prevent any part of it from going back to Europe by having goods sent here that, in spite of her handicap, Europe will be able to produce cheaper than we. And I think you and I, furthermore, are in accord that the same point of view ought to be taken when we are dealing

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with the question of our gold position and banking power. Simply because we should have neglected to organize our wealth and because we insist upon squandering our gold all over the country we should not be in a position of being niggardly or provincial when the time will come for us to do our full share in the reconstruction and further construction of the world. We should not entertain the eventuality of raising our discount rates so high that our own securities should go back to Europe, as you appear to contemplate, or so as to kill the new acceptance business with which we have begun to finance the world, and incidentally of throwing a damper on our whole home situation by a policy of rigid contraction.

Again let me say that I do not want to prophesy and ultimately such conditions may arise, but they should not occur any earlier than necessary because of our neglect to take the most elemental precautions in assembling our gold.

Even though some of the foreign loans maturing in the next years will not prove to be weapons of defence because they are secured by our own collateral which will be expected to liquidate them before they mature, we are no doubt strong enough to be able to protect

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ourselves. But, as I said, I do not believe that we want to be protectionists to a degree which would be harmful to ourselves and to the entire world because we neglected to prepare.

I believe that you will say that you are in full accord with me with respect to these objects and aims and that we differ only slightly as to the methods, and that, after all, your main objection is based upon your fear of the over issue of notes. But, as I showed you before, this over issue on a basis of 2 or 3% of till money could only be a very restricted one. Moreover, this objection could be met by limiting to a definite percentage the amount of till money kept in Federal Reserve notes. Personally, I should be satisfied to have this percentage fixed at $2\frac{1}{2}$ or 3% as against the 5% contained in our last recommendation to Congress. At the same time, I should favor beginning the tax on the notes whenever the gold cover fell below 70%. These would be two very important brakes upon any tendency to over issue on account of an excessive amount of Federal reserve notes kept in vault, but, in addition to that, you must trust to the sound judgment of the Federal Reserve Banks to keep the system safe and sound. If you have not that confidence, you could not possibly under-

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take to urge the member banks to place their excess balances with the Federal Reserve Banks. As a matter of fact there is at this time, after two years of operation, a very clear understanding on the part of the Federal Reserve Banks that their normal reserves ought to be between sixty and eighty per cent, and our system is being run on that basis.

You cite some foolish suggestions that were made by bankers from time to time as an illustration of the dangers to which the system would be exposed. I think the argument ought to be reversed. The fact that these foolish suggestions were turned down with contempt and ridicule is the best proof that, on the whole, the common sense of the banking community can be trusted. The danger remains, of course, that they may want to go far in business expansion, but there you have to rely upon the ability, intelligence and conscience of the Federal Reserve Board and the Federal Reserve Banks. If these are lacking, the country will have to pay the price whether or not the Federal reserve notes are counted as reserve. But I, for one, believe that the further we get along the better understood will be sound banking principles and the easier will it become to secure for the banks and for the Board men capable of handling the situation. The constant publicity to which the system is subjected is, in itself, an important safeguard.

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You cite present European conditions as indicating the possibility of inflation under a central banking system. I should cite them to you as proofs of the most effective instruments of protecting a country under tremendous stress. As a matter of fact, the danger in these countries is not so much from currency expansion as the tremendous growth of their national indebtedness. But that an elastic note issue under conditions such as govern Europe at this time is an absolute necessity will not be denied by you, and it is proven by the fact that even England had to take recourse to this means by issuing an unsecured government note circulation.

In conclusion, let me state frankly to you that I think you are "seeing ghosts" when you believe that Federal Reserve notes as reserve would prove to be the undoing of the regional system. Quite the contrary, it would be the making of it. It would strengthen the banks and make them independent.

You say:

> "It would be the first step toward the process of substituting the principle of centralism in our banking system for the principle of regionalism."

The principle of centralism has been introduced by the creation of the Federal Reserve Board through its power

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to make one bank rediscount for the other; through its power to regulate interest rates all over the country, and, furthermore, through the very creation of one Federal Reserve note issue which circulates all over the country without any differentiation. These Federal Reserve notes are the obligations of the United States, and the Act prescribes:

> "The said notes shall be obligations of the United States and shall be receivable by all national and member banks and Federal reserve banks and for all taxes, customs and other public dues."

Is it at all plausible to contend that this Federal Reserve note is a regional note when the law obligates all member banks all over the country to accept it? I think it is belittling the Federal Reserve System if you should consider that a step of this kind would be a "perversion of its most fundamental principle."

You furthermore say:

> "As such, I cannot but view it with the most serious apprehension. The regional principle is the vital principle in our new banking system. It is America's specific contribution to the business of reserve banking. A banking system is a growth and development, and the regional principle, which is the life giving force of the Federal Reserve System, grew out of the clearly perceived necessity of adapting the structure of any system of reserve banking which would fit American conditions to the analogies of our political and economic life and the genius of our people."

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The regional feature of our system is a necessity; not a beauty. The time may come when, after generations, our country may enjoy a central banking system as safely as do European countries at this time. In view of our political conditions and our peculiar economic conditions, a system was thought preferable that would insure a certain degree of decentralism. It is in response to this necessity that the regional system was adopted, but the creation of a system of distinct Federal Reserve Districts and Federal Reserve Banks would have been an absolute failure had they not been welded together in one strong unit by the cooperation secured through the Federal Reserve Board and by placing behind the whole system - in order to eliminate the weakness caused by the creation of comparatively unimportant Federal Reserve Banks - the great power of the United States. This led to the issue of Federal Reserve notes by the Government instead of a bank note issue as in Europe. It was done for the very reason of uniting the banks and not for the purpose of separating them. The objects and aims of those who want to further the development of this principle of regionalism must be to overcome the difficulties that are caused by the many headedness of the system; to overcome the weakness, as far as it can possibly be done, and to create the greatest possible confidence by dealing with the system as a whole

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instead of dealing with twelve distinct institutions, including some pretty weak brothers. It is from this point of view of immeasurable advantage to use this common note issue, which is backed by the strength of the United States, as a joint instrument to strengthen the whole system and to give it a power that no individual reserve bank could possibly enjoy.

The measures proposed for the strengthening of the gold and credit power of the Federal Reserve Banks are the most important steps that could be taken in that direction. They would make for the independence of the districts, and they would tend to give to the United States as a whole that great banking power that would enable us in safety to cope with the problems that lie ahead of us.

I append a folder containing some of the letters and public notices received in response to my Kansas City speech.

Very truly yours,

(Signed) Paul M. Warburg.

Hon. A. C. Miller,
Federal Reserve Board,
Washington.

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SECRETARY OF THE TREASURY
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CHARLES S. HAMLIN

H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
876.

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 14, 1916.

Dear Sir:

Some time ago it was suggested that Federal Reserve Agents bring with them to the December meeting tentative drafts of their forthcoming annual reports.

It is understood, also, that at the Third Conference of Federal Reserve Agents in Washington last June it was voted that a form should be prepared by the Executive Committee for use in drawing up the forthcoming annual reports of the Federal Reserve Agents.

As a matter of convenience there is herewith enclosed to you for reference an outline of topics which was prepared by the Statistical Division of the Federal Reserve Board last June and furnished to the Conference during its session at this time.

Respectfully,

Secretary.

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OUTLINE OF TOPICS SUGGESTED FOR TREATMENT IN THE 1916 ANNUAL REPORT OF FEDERAL RESERVE BANKS.

1. Financial results of operation:

   (a) Earnings, expenses, dividends, etc.

   (b) Comparative balance sheets for December 31, 1915 - 1916.

   (c) Profit and loss statements for 1915.

2. General business and banking conditions in the district, and activities of the Federal reserve banks during the year:

   (a) Discount operation:
   Volume of operations;
   Discount rates;
   Classification of paper handled by maturities;
   Commodity paper;
   Two-name paper (trade acceptances)

   (b) Acceptance business:
   Volume;
   Rates;
   Classification by maturities;
   Domestic acceptances.

   (c) U. S. bond operations:
   Open market purchases;
   Transactions through the Treasury;
   Conversions;
   Sales;
   U. S. notes.

   (d) Municipal warrants:
   Volume of paper bought;
   Rates;
   Maturities;
   Classification of securities by character of issuing public bodies.

   (e) Changes in the reserve position of the bank during the year.

3. The Federal reserve bank and member banks.

   (a) Changes in membership due to transfers from and to other districts;

   (b) Movement of membership within the district;

   (c) Relation to national banks, State banks and trust companies;

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(d) Accommodation of member banks through discounts;

(e) Member bank deposits;
Excess deposits;
Overdrafts.

(f) Periodic reports regarding condition of member banks;
Examination.

(g) Bank failures within the district;

(h) Overdue paper.

4. The Federal reserve bank and the public.

(a) Open market operations of the Federal reserve bank;

(b) Effect of the discount rate policy of the bank upon general market rates;

(c) Publicity work of the bank, and the attitude of the public toward the Federal reserve system.

5. The Federal reserve bank and the Government.

(a) Government deposits;

(b) Relation to the U. S. Treasury;

(c) Relation to the Comptroller's office;

(d) General considerations.

6. Federal reserve banks and note issues.

(a) General policy in the matter of note issues;

(b) Substitution of Federal reserve notes for gold as circulating medium;

(c) Cover of notes issued;

(d) Denominations of notes issued;

(e) Average life of notes issued;

(f) Inter-district movement of notes;

(g) Redemption and destruction of notes;

(h) Cost of Federal reserve notes;

(i) Federal reserve bank notes;

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(j) Federal reserve agents and note issues;

(k) Amendment regarding note reserve.

7. Internal management of the bank.

(a) Functions and work of directors, executive committee, etc.;

(b) Changes in the personnel, and in the organization of the department, including the Federal reserve agent's office;

(c) Office and vault facilities;

(d) Examination by Federal reserve examiner.

8. The clearing problem.

(a) Clearing to July 15, 1916;

(b) Clearing after July 15, 1916;

(c) Service rendered to the banks by the Gold Settlement Fund.

9. Conclusion.

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Remarks of H. Parker Willis, November 22, at Paterson, N. J.

MEMBERS OF THE SECOND NATIONAL SILK CONVENTION.

Gentlemen:

You have asked me to speak to you about "The Federal Reserve Act in its Relation to the Manufacturer." I am happy thus to have the opportunity of presenting one aspect of a great business question to a national organization like your own. Much has been done within the past few years by national organizations of business men who have addressed themselves to the solution of broad problems affecting industry in its relation to the country at large. A good deal of our future development will depend upon the continuation of this organized effort. It has been found in most lines of manufacturing and business that beneficial changes follow and abuses yield far more quickly when they are dealt within consequences of a united expression of opinion preceeding directly from the general mass of those affected by the proposed action, than they do when they are the subject of analysis and discussion merely by individuals and expert authorities, however able these may be. It is, in short, largely the result of the effective and public spirited work done by organizations of producers within the past few years, that so much progress has been made in national legislation affecting trade conditions.

Such organization and cooperation in the study of economic questions has at last extended, I am happy to say, to the point where it it involves association and cooperation between the business public on the one hand, and Government authorities on the other. The Federal Reserve System is the outcome of such work, and is probably the measure

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whose bearing on our economic welfare is broadest, since it has no special relation to the work of one set or group of business men more than another. It is a great piece of national legislation; and its greatness is found in this very fact, that it deals with a question in which all are interested, and interested in much the same way. I have often been asked to explain the effect of the Federal Reserve Act upon the farmer, or upon this or that branch of business, and have always replied that the effect of the law upon one is not different from its effect upon another - that it is, in short, a measure intended to improve business conditions, lay the foundations for more efficient service, render credit uniform in its distribution among borrowers of equal merit, and reduce the cost of production of every article of manufacture, and of every service to the community, by rendering sound assets more readily convertible into immediate means of payment, irrespective of origin, ownership, or the special purpose of their creation.

In another sense, however, every branch of business has its own problems of credit and banking directly affected by the Federal Reserve Act, because industries are in different degrees well organized with respect to banking credits, and in different degrees habituated to the use of simple and economical means of securing advances. It may be said, therefore, that you are doubly interested in the working of the Act: first, because you are active members of the business community, and, as such, have a vital interest in the Act irrespective of the particular problems of your branch of business; and secondly, because the special usages and conditions surrounding the movement of your goods from producer to consumer may be improved at certain points by taking full ad-

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vantage of the opportunities held out under the new law.

Thus far business men have taken too slight a direct interest and share in the working of the Act. It is in no sense a disparagement of the Federal reserve banks to say that hitherto they have been essentially bankers' banks. Indeed, this appellation is frequently given to them in so many words, and they are described as being in theory, as well as in fact, banks for keeping of bankers' funds. This, however, is an erroneous view of their functions. It is true that the Federal reserve banks have not, and under the Act as it now stands, never will have, direct relations with individuals as depositors and borrowers. That is a peculiar feature of their organization, due to the special reserve character of the banks. They are organized as the holders of banking reserves, and that is their primary function. A secondary, although almost equally important function, however, is that of influencing the discount market, and of making an official discount rate effective therein. This is a function exercised in every country by the reserve holding institution or institutions in existence there. The purpose of it is to affect the market for the higher classes of commercial paper by putting funds into or withdrawing them from the field, as circumstances may require, thereby regulating discount rates, rendering them more stable, and, when necessary, exercising a decided influence upon the gold supply of the country. It was recognized by those who framed the Federal Reserve Act that the exercise of this function would be absolutely necessary in the United States just as it is abroad, if the reserve banks were to fulfill the full measure of their duty. Consequently the act provided that they might go into the open market, dealing not merely with their stock-

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holders and depositors, but with any individuals, firms, corporations, or banks they might choose, in order to render efficient and satisfactory service. The fact that up to date the Federal reserve banks, except within a few limited fields, have not availed themselves of their open market powers, and have practically not availed themselves of them at all in so far as relates to the direct purchase of business paper, is largely due to the difficulty of organizing and setting in operation a great system with all of its functions in full effect. Time is needed for such development. It has been necessary to perfect the working relations between Federal reserve banks and their members before going actively into the paper market. The time, however, has come when the open market function of Federal reserve banks will soon be called into active play. It largely rests with the business man to determine just when and to what extent the Federal reserve banks shall become direct buyers of his paper. The banks, as I have said, are already permitted, under the regulations of the Board, to engage in this business. If the manufacturer desires that they should undertake it actively, it is within his power to hasten the time when they will do so. I look forward to the day when the Federal reserve banks will bear to the American paper market very much the same relation that was borne before the outbreak of the present war by the Bank of England to the British discount market. If, as the result of changes due to the war, America should succeed in obtaining something of the influence possessed by Great Britain in international financial affairs prior to the coming on of the European struggle, this would mean that the Federal reserve banks might bear to the discount market of the

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world a relation like that which existed between that market and the Bank of England. It is a great and brilliant place which may thus be taken by the reserve banks, but in order to take it, they need the assistance and cooperation of the business man, particularly of the business man who is engaged in international operations upon a large scale, or in the domestic shipment and sale of staple commodities. It was because of the belief that the business man would entertain a direct and vital relationship to the Federal reserve banks in the way I have described, that the Federal Reserve Act provided for a special element among the directors of each Federal reserve bank, comprising one-third of the membership, which was to consist not of bankers, but of business men. It is the hope of every student of the system that as time goes on these business men's places upon the directorates of Federal reserve banks will be increasingly sought by business men of the highest ability, and that they will look to them as properly belonging to the best and most representative members of the commercial community, and to be distributed accordingly. At the present day our merchants and producers are too much inclined to look upon Federal reserve banks as a part of a technical banking mechanism, and to regard service in connection with them as no doubt an important public duty; but nevertheless one which can have only an indirect relationship to individual business. This is a view which calls for broadening and clarification. There is no more important mechanism in the country not merely in its bearing upon underlying financial conditions, but in its significance to the actual credit and prosperity of every individual business concern, than the Federal Reserve Bank. It is, therefore, the duty of the owner and operator of

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business enterprises to share in the operation of the reserve bank, and to regard his participation therein as a fulfillment of an essential obligation to the commercial world of which he is a part. Only by this process can the Federal reserve banks be taken out of the narrower field of technical banking, and brought into the larger field of commercial operation, and so be made to yield their highest results both to the banks and to the world at large. As I have already said, and as I now wish to emphasize, the time has come when definite steps in this direction must undoubtedly be taken; and these can be taken only through the effective aid and cooperation of the manufacturer and dealer.

Without, however, anticipating the development of the new system, and without awaiting the larger participation of business men in its operation, the Federal reserve system has already assumed a most important, practical relationship to business. In three ways the active business man or manufacturer, whoever he may be, or in whatever line of production he may be engaged, is directly interested in the working of the Federal Reserve Act. First of all the Federal Reserve Act has provided a new and effective means of financing importations and exportations of goods, thereby reducing the cost of such financing. Second, the Federal Reserve Act has provided an effective means of securing accommodation in domestic business, thereby reducing the cost of the movement of goods from producer to consumer. Third, the Federal Reserve Act has provided a prompt, economical and satisfactory means of collecting the checks and drafts that come into the possession of the business man.

The financing of importation and exportation is of particular importance to an industry which depends so largely upon imported raw

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materials as does the silk business, and which is of late years beginning to find so large a market abroad for its completed products. By providing for the introduction of the bankers' acceptance, the Federal Reserve Act has made it possible for importers in the United States to obtain their accommodation upon a very low cost basis. Instead of applying to their own bank direct and getting a loan based upon their own discounted paper whose proceeds are to be used in paying for goods brought from abroad, the importer can now arrange for the opening of a credit at his bank, the banker accepting for him, and the draft as thus accepted, being readily saleable in the discount market. Some progress has been made during the past year in developing this method of financing our foreign trade. It is estimated by the Federal Reserve Board's statistician that the total amount of acceptances now outstanding is at least $175,000,000, of which about $100,000,000 has been made by New York banks and bankers. Decided progress has also been made in other cities, and the new mode of financing has already undoubtedly earned a permanent place for itself in our credit system. The Federal reserve banks within the past year have purchased freely of such acceptances at rates averaging less than 2½%.

The extent to which your own particular branch of business is interested in this development may be gathered from figures which I have had compiled to show the actual dealings of Federal reserve banks in paper based upon the importation of silk. As you probably know, each Federal reserve bank reports daily to the Federal Reserve Board the nature of its transactions and the character of the operations out of which they grow. A condensed summary of such reports shows that during the months

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of September, October and the first half of November a total of paper aggregating $5,584,658, growing out of importations of silk, was bought by Federal reserve banks. Of this sum $3,769,600, was bankers' acceptances, while $1,815,957 was classified as trade acceptances. You are doubtless aware, that the trade acceptance, under the regulations of the Board, is a bill of exchange drawn by a seller upon a buyer, running not more than 90 days sight, accepted by the buyer, and growing out of actual sale and shipment of goods. These trade acceptances have been discounted by Federal reserve banks at a special rate established under regulations of the Board, ranging from 3½% to 4%, while, the bankers' acceptance ranges from 2% to 4%, and the actual purchases during the past year have as already noted been made at rates averaging less than 2½%. From 2½% to 3½% may thus fairly be stated as the average level at which Federal reserve banks have financed the importation of silk into the United States, as shown by the figures I have already cited in gross, and which may be furnished in detail for each Federal reserve bank as follows:

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AMOUNTS OF BANKERS' AND COMMERCIAL BILLS BASED UPON SILK IMPORTATIONS, ACCEPTED BY AMERCIAN BANKERS AND IMPORTERS AND BOUGHT BY FEDERAL RESERVE BANKS DURING SEPTEMBER, OCTOBER AND NOVEMBER 1916.

	BOSTON	NEW YORK	PHILADELPHIA	CLEVELAND	RICHMOND	ATLANTA
Sept.						
Bankers	62,803.67	188,578.40	169,197.79	130,433.06	... .	36,451.47
Trade	. ... ..	448,664.82	186,905.62	132,604.07	... .	. ... ..
Total	62,803.67	637,243.22	356,103.41	263,037.13	... .	36,451.47
Oct.						
Bankers	. ... ..	508,516.07	236,974.69	364,376.68	... .	. ... ..
Trade	. ... ..	121,027.75	3,102.51	7,632.32	... .	. ... ..
Total	. ... ..	629,543.82	240,077.20	372,009.00	... .	. ... ..
Nov.						
Bankers	. ... ..	382,129.57	21,487.43	113,352.14	... .	. ... ..
Trade	. ... ..	109,193.02	25,111.67	22,049.31	... .	. ... ..
Total	. ... ..	491,322.59	46,599.10	135,401.45	... .	. ... ..
GRAND TOTAL						
Bankers	62,803.67	1,079,224.04	427,659.91	608,161.88	... ...	36,451.47
Trade	. ... ..	678,885.59	215,119.80	162.285.70	... .	. ... ..
Total	62,803.67	1,758,109.63	642,779.71	770,447.58	... .	36,451.47

Continued on page #10.

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	CHICAGO	ST. LOUIS	MINNEAPOLIS	KANSAS CITY	DALLAS	SAN FRANCISCO	T O T A L
Sept.							
Bankers	39,979.91	58,058.07	.. ..	22,160.33	.. ..	96,151.13	803,813.83
Trade	. ... ..	. ... ..	28,178.03	. ... ..	.. ..	150,347.18	946,699.72
Total	39,979.91	58,058.07	28,178.03	22,160.33	.. ..	246,498.31	1,750,513.55
Oct.							
Bankers	274,596.04	221,762.03	97,543.36	31,146.55	.. ..	319,224.26	2,054,139.68
Trade	20,000,00	. ... ..	. ... ..	. ... ..	.. ..	491,193.93	642,956.51
Total	294,596.04	221,762.03	97,543.36	31,146,55	.. ..	810,418.19	2,697,096.19
Nov.							
Bankers	21,006.55	41,871.14	20,331.48	28,431.12	.. ..	283,037.52	911,646.95
Trade	50,499.21	. ... ..	18,548.26	. ... ..	.. ..	. ... ..	225,401.47
Total	71,505.76	41,871.14	38,879.74	28,431.12	.. ..	283,037.52	1,137,048.42
GRAND TOTAL							
Bankers	335,582.50	321,691.24	117,874.84	81,738.00	.. ..	698,412.91	3,769,600.46
Trade	70,499.21	. ... ..	46,726.29	. ... ..	.. ..	641,541.11	1,815,057.70
Total	406,081.71	321,691.24	164,601.13	81,738.00	.. ..	1,339,954.02	5,584,658.16

NOTE: Acceptances mostly drawn by Japanese exports.

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Remembering that the average monthly importation of raw silk into the United States is approximately $10,000,000, the service which the Federal reserve banks are beginning to render in connection with this branch of business, is readily appreciated. This, moreover, is only the beginning of what may be done by the reserve banks with cooperation of the various commercial institutions interested in opening our foreign credit. They can enlarge the business and perform for others the same service which they are already rendering to those who have known how to take advantage of the new facilities. Not only this, but the Federal reserve banks can, and in the future undoubtedly will, extend their scope of operations in trade paper directly to the importer and business man. The paper of which I have already spoken as having been accepted in connection with the importation of silk, has in practically every case been purchased with the endorsement of some bank, or after having been accepted by a bank, but in any case with a bank's name upon the paper - a guarantee for which the merchant himself has, of course, had to pay. As I have already suggested, it has been necessary that Federal reserve banks should develop this new line of business slowly and with care, and that they should not embark upon the individual paper market too early. Nevertheless the question of their doing so is only a matter of ascertaining the real facts as to the credit of individual concerns. Both under the Act and under the regulations of the Board there is no reason why they should not deal direct with individuals to any extent that they may feel disposed. There is no reason, therefore, why importers of staple raw materials from abroad should not take advantage of this new and cheap mode of obtaining credit.

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Very great advantage has already accrued to the importing community by reason of the steps taken in the direction of a wider use of bankers' acceptances, but what has been done thus far must be considered only a beginning. Bankers have been slow to take advantage of the new method of financing the importer, and later he has been equally slow in urging them to assist him by availing themselves of the credit facilities within their reach. It is possible, too, that this slowness is in no small measure due to the abundance of funds that have been in the hands of our banks during the past two years, to the fact that our interest rates were far lower than those prevailing in other markets of the world, and that in consequence of these conditions the legitimate business man has had no trouble in getting any reasonable amount of credit that he desires, at rates distinctly lower than he has enjoyed heretofore. This is a condition that will not always endure, and when the time of greater pressure arrives, as it will, the importer will find it to his interest to avail himself of every means of cutting down the cost of his banking accommodation. He will, however, save himself much delay and inconvenience at that time if he will, during the period when credit and cash are abundant, take pains to show his banker that he is interested in the adoption of modern methods of doing business, and of economizing in the cost of loanable capital.

The second phase of the manufacturers' relation to the Federal Reserve Act is, as I have already mentioned, found in the provisions made by the Act for the cheaper financing of domestic trade through the purchase of paper growing out of domestic sales and shipments. In the original Federal Reserve Act Federal reserve banks were authorized both

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to discount and to buy in the open market ordinary bills of exchange of short term maturities growing out of real business transactions. The Federal Reserve Board established a special low rate for trade acceptances, that is to say, accepted bills drawn by one merchant upon another, or by a manufacturer upon a wholesaler or a retailer. Congress on the seventh of September 1916, carried this plan to its logical conclusion by authorizing the banks to accept paper growing out of domestic trade operations, and involving the purchase or sale of staple goods s stored in warehouses and used to protect the acceptance. Little more than a year has passed since the Board's circular relating to trade acceptances was issued, yet during that time Federal reserve banks have held at times as much as $4,400,000, of such acceptances bought in the open market, while the total volume afloat in the country at large, although it can not be stated even approximately, is undoubtedly very considerable. Less than three months have passed since Congress authorized the acceptance of properly documented paper growing out of domestic operations. There has thus not been time as yet, either to introduce the domestic documented acceptance very widely, or to obtain reliable statistics with reference to it; but it is certain that many of the large financial institutions members of the Reserve System are already advocating the use of it, and I know that some of the ablest banks throughout the country are making extensive and carefully framed plans for the financing of trade based upon this new pow power. The domestic acceptance will be of great interest to every class of producer, but to none more than to the manufacturer. He will

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have a double duty in seeing to it that such acceptances are kept within the proposed meaning of the law by confining them to bona fide documentary drafts growing out of actual sales, and by insisting that so far as possible, his banker shall cooperate with him and with his customer in the use of this plan. It will also be his duty, so far as he can, to urge upon those who buy from him, the use of the trade acceptance in lieu of the open account system, either with or without a cash discount feature. There are on this side of the matter some difficulties to be met and perhaps some hardship to be incurred at the outset. Wherever there exists a highly protected industry catering to a public with whom prices are not a primary consideration because the article is one ordinarily classed as a luxury, there is an inevitable tendency to long-term credit whose cost is covered by higher prices, maintained on a basis intended to provide for losses due to poor collections and unsatisfactory credit conditions generally. And yet this is exactly the condition that ought to be guarded against. You can retain your market better by maintaining your efficiency, keeping your prices reasonable, your quality high and customers consequently satisfied; and these objects can best be attained when poor credit is carefully eliminated, and when goods are sold on a basis that calls for prompt payment when due. It may be difficult at first to induce buyers to assent to the trade acceptance plan with all that it entails, yet this should be entirely possible after a very reasonable period of education. If your association would go on record in behalf of the trade acceptance method of settling accounts, a long step would have been taken toward the elimination of the initial inertia which tends to obstruct progress.

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In this connection let me cite the following clear cut summary by Deputy Governor Calkins of the Federal Reserve Bank of San Francisco, of the reasons why the trade acceptance should be adopted by the progressive business man as a method of financing his business:

"First - The present trade conditions in this country are conditions of undefined credit inaccurately applied to the trade of the country.

Second - These conditions should be reformed by the substitution of defined credit and certain terms.

Third - This reform may be brought about by the rigid application of the sound principles of trade credit, by extending trade credit only to operations in goods - that is, applying trade credit to trade.

Fourth - The trade acceptance is the best credit instrument yet devised for applying trade credit to trade, and because of its simplicity and adaptability, its general use will radically improve conditions of trade credit, thereby facilitating trade.

The use of an acceptance in closing a transaction involving deferred payment for goods purchased enhances the credit of the accepting purchases and facilitates the financing of the sale by the seller.

The credit of the acceptor is enhanced by the evidence that he is buying on certain terms, is prepared to pay at a certain time and is adopting the most approved and economical method of transacting his business.

The seller is benefited by securing a piece of prime commercial paper, carrying the responsibility of two merchants, covering a genuine, live transaction, and consequently discountable, at the most advantageous rate, thereby enabling him to sell on better terms without decrease of profit.

Each is contributing his share toward placing mercantile credits on a sounder and more stable basis involving fewer losses, less uncertainty, and great improvement over the prevailing practice of buying on open credit."

The agrument in favor of the use of the trade acceptance is so simple and so obvious, that it would be a discourtesy to the intelligence

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of a body like this to attempt to urge it further. Only in the fact that it runs counter to certain trade practices can there be found any reason for failure to apply it without further delay. I have noticed in the Rules to Govern Transactions Between Buyers and Sellers of Broad Silks in the United States of America, the following terms:

R U L E O N E .

Selling Terms shall be six per cent, ten days, sixty days dating.

This means that bills are due and payable at the office of the seller, less a discount of six per cent, in seventy days from the date of the invoice, the buyer having the privilege of anticipating the sixty days at the rate of six per cent per annum, within ten days from date of invoice (which ten days are not discountable).

R U L E T W O .

Overdue Bills shall be paid upon the basis of a reduction in rate of discount, from the rate of six per cent stated above, of one per cent for each thirty days or fraction thereof beyond sixty days from date of invoice, and having become due net, shall be subject to an interest charge of six per cent per annum.

Further in the rules and regulations to govern transactions in the silk trade of the United States, as approved by your own association, I find the following description of the selling terms on which members of the association are expected to operate:

The recognized rate of discount in the silk trade is six per cent per annum when not otherwise stated or agreed.

Offers of silk when not otherwise stated imply:

6 months basis for Asiatics.
60 days basis for Europeans.

Six Months' Notes, 4 Months' Notes, 3 Months' Notes, or 60 Days' Notes. Such sales convey no right to discount. Within 30

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days from date of bill, Buyer must give his note for the period specified, bearing same date as bill, drawn to his own order, blank endorsed and payable at discretionary points as defined by New York Clearing House.

Six Months' Notes, or Cash Less 3 Per Cent, implies the right of Buyer to pay his bill within 10 days (which are not discountable) by deducting 3 per cent from the face thereof; otherwise he must give 6 months' notes from date of bill as above provided.

Four Months' Notes, or Cash Less 2 Per Cent, are governed in principle by the above terms.

Ninety Days' Notes, or Cash Less 1½ Per Cent, are governed in principle by the above terms.

Ninety Days, Sixty Days, or Thirty Days - required that the bill must be paid within the time specified.

Six Months' Basis, Payment Within 30 Days, or 60 Days or 90 Days (as written) requires payment at any time within period stated, with discount for unexpired portion of the six months.

Six Months' Basis, Settlement by Note or Cash Within 30 Days, or 60 Days, or 90 Days (as written) gives Buyer the option of paying (at any time within the stipulated period for settlement) in cash less discount for unexpired portion of the six months, or giving (at any time within the stipulated period for settlement) his six months' note from date of bill.

Cash Sales less a stipulated discount require immediate payment of the bill less the specified discount.

Bankers' Credit Sales require the Buyer to immediately furnish approved Credits at the usance agreed upon in the transaction. For such sales the Seller takes no responsibility for arrival, damage, loss or pilferage en route. Seller's failure to demand the Letter of Credit shall not be cause for voiding the contract.

It would be far better if in lieu of this plan for establishing a fixed term of credit upon open accounts, with cash discounts, there could be introduced the trade acceptance system of which I have spoken. The change would, of course, involve some difficulty at the outset, but

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its value would be infinitely great as compared with the very limited sacrifice involved. What progressive business concerns think of the innovation I am urging upon your attention may be seen from the following expression conveyed in a letter from the Thomas A. Edison Company to the Federal Reserve Bank of Cleveland:

> "We will no doubt meet with the same objections as other concerns are receiving in the endeavor to introduce this new business custom, but we are going to put our energies forth in the hope of making it universal with our trade."

What the Edison Company has found good and desirable in the management of its credit relations, will be found equally good and desirable by others; and this is but one of the many energetic and enterprising business houses that are taking active steps to place their operations upon the basis which has been found by the most advanced commercial countries to be advantageous.

The trade acceptance plan must not be interpreted as a means of extending assistance to weak houses which would otherwise be unable to obtain credit. Were it to be so applied or interpreted, its purpose would entirely disappear. Mr. George H. Paine of Philadelphia, whose work in popularizing the trade acceptance is probably well known to you, remarks in substance on this point:

> Neither producer nor jobber is interested in any method that encourages customers to lean upon them for financing in the way that ordinary notes and the old forms of acceptance have led them to do in the past. They feel that to encourage a customer who is unable to obtain the aid of financial institutions to finance himself, extending their own credit to him in lieu of the aid of such institutions, is to encourage unfair competition, and to bring about other unsettling conditions. Business has passed beyond the primitive period when producer and jobber had to finance their own customers, because no financial institutions were available to do the work.

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> It is today, however, the duty of the producer and jobber to aid the customer to obtain that credit to which he is entitled from financial institutions, and at the same time to aid these institutions themselves in granting credit by supplying with each transaction in which they engage such data or evidence of its true nature as may be needed in determining the credit growing out of the transaction. Men of all industries are eager to cooperate in any plan or method that carries out this idea.

Can not the trade acceptance plan be more fully adopted in the silk industry? It is, as usual a question of introducing an efficiency device, leadership and willingness to introduce new methods that are called for and, these granted, the results are certain, for the Federal Reserve Act and the regulations of the Federal Reserve Board have prepared the ground for a firm and safe advance.

I have spoken of a third way in which the silk manufacturer is particularly interested in the operation of the Federal Reserve Act because he is a manufacturer and a business man, and not because the matter I refer to has any special bearing upon his particular product. This is the method provided by the Federal Reserve Act for collecting checks, drafts, and other current obligations drawn on banks. It was an essential and integral feature of the original Federal Reserve Law that it provided for the introduction of a general and effective clearance system. It has taken some time to work out such a system in application, but the difficulties in the way have been at last surmounted, and the Federal Reserve Board has established at each Federal reserve bank a plan whereby checks are collected without an exchange charge, not only upon national, but also upon many State banks. The total of such banks now cooperating with the system is about 15,000. Largely as a result of it, many of the clearing house associations of the country have mod-

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ified their scale of charges to customers or their regulations relating to the collection of checks. No detailed figures can as yet be given, but it is safe to say that the cost to the merchant and manufacturer of transacting business has been curtailed by a very large sum each year. The business man is today able to secure the collection of his checks entirely free if he is willing to wait for the return of funds, or at a very moderate charge based on recognized principles of cost, if he desires immediate use of these funds. The progress and success of this system, which is now under attack from various persons who feel that it tends to reduce their profits, will depend very much upon the support it gets from business men who recognize the influence it is having upon their actual operating cost, and who do not hesitate to express themselves in favor of efforts made in their behalf. by the Federal Reserve Board in accordance with the provisions of the law. This is the first effort ever made in the United States towards the introduction of a scientific, simple system for collecting the business man's claims against others, and relieving him of the unnecessary expense hitherto visited upon him in various parts of the country. when, on account of competitive conditions, he has been obliged to absorb the cost of getting in payments which should have come to him in full.

Apart from the problems of handling foreign and domestic business in silk which may be solved by the aid of the Federal Reserve banks along the lines that I have just described, is the general question of the organization of foreign trade in its relation to banking and finance -

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a matter of primary interest to the manufacturer whether we view him as a consumer of imported raw material, or as a shipper of finished products to foreign customers. The Federal Reserve Act which has touched so many fields of business, has provided for a profound change in this one, not merely through the development of better forms of commercial paper, but also through provision for change in organization. It has not only authorized national banks to establish branches abroad under liberal conditions, and permitted groups of national banks to join together for the purpose of forming other institutions primarily interested in foreign trade, but it has also provided for the establishment of agencies of Federal reserve banks themselves. The working out and application of this system of foreign banking and finance is fundamentally important to the American manufacturer who either wishes to be assured of steady and regular supplies of raw material, or of the proper placing of his goods on the foreign market at reasonable expense. Manufacturers in general, therefore, are profoundly interested in the reorganization of the foreign side of our banking system which is called for in the Federal Reserve Act.

The silk manufacturing business as such, moreover, is peculiarly concerned in the mainentance and development of foreign trade upon a sound and satisfactory footing. The raw silk markets of the Orient are of special significance to your industry, and this amounts to saying that everything which affects the condition of credit and the methods of business with those markets, is of immediate concern to you. High rates of exchange and difficult banking and shipping conditions throughout the East have impeded business with Oriental markets and

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threaten to continue to do so for a good while to come. The shipping situation will be corrected comparatively slowly, but there is no reason why banking credit and exchange conditions in the East should not promptly be improved. I have had a small part during the past few months in the effort to place these conditions upon a sounder basis, and to bring the importers and exporters of the United States into a more satisfactory and economical relationship with at least a section of the Oriental market, and have been deeply impressed with the lack of progress in the use of modern banking methods in the Orient. No one who visits the far East can help being struck by the extremely limited extent to which American institutions and American capital have taken root there; and the current explanation for it is that for many years past Americans have found it more profitable to invest their funds at home than to put them into manufacturing, distributing or banking in the East. We could understand such statements if it were true that the Orient constituted a separate part of the world, entirely disconnected with the United States or with the West generally. Such, however, is, of course, not the case. We have a vital interest in Oriental trade. It is undoubtedly the duty of the manufacturer to help in this development in two distinct ways - first, by encouraging the formation of foreign trade institutions under American control; and secondly, by encouraging and placing his business with such institutions or with those organized by Americans in foreign countries which have a genuine and direct interest in enabling the American producer to hold his market, and in assisting him to cut his cost of importation and exportation. I regret to say there are at the present

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time many American manufacturers who seem to prefer dealing with foreign banks on the ground that these foreign institutions have an established clientele, known practices in business, and well established connections. These facilities for transacting business are, however, readily acquired by any well organized American institution. By assuring such institutions of a reasonable volume of business, and by encouraging the entry of the Federal reserve banks into the foreign field, we can arrange for the financing of our operations in other countries as quickly and as readily as we have during the past two years popularized our goods themselves in those countries.

In closing this very brief outline of your relations to the Federal Reserve Act, let me again, at the risk of repetition, emphasize what I have already suggested at an earlier point. The Federal Reserve Act, is of far more interest to the commercial establishment than to the banker, if such a thing can be. Federal reserve banks can, and in due time will, establish direct relations with the business house, buying and selling its paper, particularly when such paper has been accepted by a bank. It is at present on the business houses of the country that the chief reliance for the working of the more beneficial features of the measure, for the further development of the discount market, and for the evolution of the new business customs necessary in order to bring our business practices into harmony with those of other countries, must be placed. Because of the fact that the Federal Reserve Act does not provide for the direct performance of ordinary banking functions for individuals and firms by Federal reserve banks, it becomes necessary for those concerned to exert

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themselves actively in recasting the credit and commercial methods of the country in order to take to themselves the benefits which would otherwise be in danger of lying dormant. This a mode of approaching the situation which calls for some vision and imagination, and, above all, for some cooperative effort on the part of those affected by it, but given these qualities, the benefits of the Act are not difficult of attainment. There has been in the past too much vague and general approval of the Federal Reserve Act among business men, and too little direct effort to apply it and to profit by it. The business community has been content with the negative benefits of the law - so content as to call for little of the positive help that the Act can easily supply, as well as less than the community has a right to expect. Future development, it is to be hoped, will change this condition of affairs, and will bring the business community into active and direct cooperation with the Federal Reserve Board for the purpose of introducing in the several trades and branches of business the new forms of business paper, and of encouraging their presentation and sale both to member banks and to Federal reserve institutions.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 21, 1916.

My dear Mr.

On behalf of the Federal Reserve Board's Committee on Clearing, I want to ask you some questions and make some suggestions about progress in the clearing operations and what steps, if any, should be taken to promote the enterprise. It would appear that while the progress was very good in the first sixty days, we have now come to something rather like a standstill.

It appears, through the operation of rules adopted by banks in most of the clearing house cities, that the non-member banks and banks not agreeing to remit at par, are reaping practically the same benefit from the arrangement as those who are members and whose cash is invested in the Federal Reserve Banks. For example, a non-member bank can, if it cares to, operate through a member bank, get all its items on the banks that remit at par cleared through the Federal Reserve Bank at a nominal expense.

The customer is receiving very slight benefits from the introduction of the system. I have found, for example, in a number of the large cities no charge is made on the checks of

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customers, regardless of the banks upon whom drawn, while in other cases the same charges as were formerly made are in effect and no differential is made to the customer in favor of a check drawn on a member bank, or on a bank agreeing to remit at par through the Federal Reserve Bank.

I do not see how we are going to increase our clearing operations very materially, or add to our par list, unless we can give some inducement to the member bank; (1) for using our facilities; (2) to the State bank that remits at par over the non-member State bank that refuses to remit at par; and, (3) we will continue to get complaints from merchants, manufacturers and jobbers unless we can secure for them a substantial share of the advantages from the reduced cost of collections through Federal Reserve Banks.

At the present time Boston is collection for its members checks drawn on every bank in its own district. San Francisco is doing the same, though, in the case of San Francisco, the collection is made in some cases at considerable expense through the agency of express companies, or in such other way as may be necessary or expedient. The Federal Reserve Bank of San Francisco is thus rendering a very valuable service to its members, because it is taking from its members checks drawn on any city in the district and collects them as

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best it may. If, in doing this, it were to establish a differential rate, say 1½¢ for checks on banks that remit at par and a charge sufficient to cover expense on checks drawn on banks not remitting at par, I think they would increase their par list rapidly and if, by the same token, you could induce your city bankers to establish a differential charge between checks collectable through the Federal Reserve Bank on a nominal charge and those not so collectable, you would rapidly add to your par list, by pointing out to the depositors the advantage of dealing with banks whose checks are collectable at par through the Federal Reserve Bank. The action of the Kansas City and Omaha banks, and the St. Paul and Minneapolis banks has been along this line, and has resulted in adding more banks to the par list than all the other Federal Reserve Banks combined.

Another suggestion which comes up for consideration on the recommendation of one of the Federal Reserve Banks is the right to pay a member bank a fee for collecting items drawn on non-member banks in its neighborhood. This suggestion was embodied in the original proposal made by the Clearing Committee to the Governors and it is believed to be absolutely sound in principle. Just what would be fair compensation in various circumstances and how it should be applied remains to be worked out. In cities big enough to maintain clearing houses there is

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no object in having such a rule, because the Federal Reserve Bank can operate through any member bank that is a member of the clearing system, but where we are asking a member bank to collect from non-member banks, a moderate compensation fee would certainly be entirely justifiable and would be one means of giving country member banks some reward for their membership in the Reserve System. The payment to a member bank of a small fee for collecting non-member bank items must not be confused, as some of the Governors have done, with the payment of an exchange charge to the remitting bank. Our whole collection plan is based on the proposition that a check is payable in cash at the counter of the bank upon which it is drawn. However, that check is presented, the bank paying the cash has no right to deduct anything from the face of the check. We pay the cost of remitting cash if cash is necessary, or we accept suitable exchange or offsetting items. If we ask Bank "A" to send its messenger to Bank "B", whether he be a mile off, or ten miles off, some fee for rendering this service and remitting the proceeds is certainly justifiable and proper and, in the opinion of the Clearing Committee, would go a long way toward rounding out our System.

If this idea, as above explained, were coupled with the San Francisco plan of accepting from member banks checks drawn on every bank in the district, whether that bank has

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assented to remit at par or not, it would make rapid strides toward the adoption of a universal clearing system. The customer of the bank would then sort his checks in two columns, in one column checks drawn on banks collectable at par through the Federal Reserve Bank; in the other column checks which can only be collected at more or less expense, and upon which some arbitrary fee of perhaps 1/8 or 1/10 might apply.

Your early consideration of all these suggestions will be very much appreciated and I may say that I am in hopes that you will come to the meeting of Governors in December with some concrete proposal calculated to meet the points herein offered and if there are objections to carrying out the suggestions made that you will offer some adequate substitute.

Yours very truly,

Chairman, Committee
on Clearing.

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STATEMENT FOR THE PRESS.

November 21, 1916.

The Federal Advisory Council, which closed its regular quarterly session here today, devoted its attention to a survey of business conditions throughout the country, to reserve conditions in the several districts, and in this connection, to a consideration of the situation produced by the large and continuing imports of gold.

The Council considered means for making effective in a greater degree the transfer of vault money by member banks to their respective Federal reserve banks - a process rendered possible by the recent amendment to the Federal Reserve Act. It was agreed that this is a desirable development and that it should be encouraged.

The Council announced itself as in entire accord with the views already expressed by the Board, suggesting caution and moderation in the use of those credits which, being open for a long period of renewals, lose their character as essentially self liquidating transactions of short maturity.

The Council renewed its recommendation that the National Bank Act be amended so as to enable National banks in reserve and central reserve cities to establish branches within those cities.

Another recommendation made by the Council was to ask Congress at its approaching session to amend the Federal Reserve Act so as to provide that the final steps specified in the Act be taken early in the year 1917 instead of in November of that year as now provided, so that balances with reserve agents should cease to be counted as reserve after February or March 1917. This change would reduce materially the present excess reserves, and the so-called "reserves" now kept by country banks with correspondent banks, would henceforth be considered properly as bank balances only.

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This is a change which under the law must be made not later than November 16, 1917. In the opinion of the Federal Advisory Council and of the Federal Reserve Board, it could be effected now or in the near future without inconvenience and to the real benefit of the country. Both bodies agreed that it would be highly desirable to make this change at a time when we are certain that it can be done without any shock or jar, and when the increase of real reserves with the Federal reserve banks, would be so effective in strengthening the control of the country's gold supply, and would at the same time minimize any apprehensions that might be felt because of its increasing volume.

While all members of the Council reported excellent business conditions in their districts, statements were made that here and there some indications of increasing demand for credit facilities are to be noted, as well as a tendency on the part of some banks towards over investment of funds.

Members of the Board and of the Council expressed the view that there are no dangers that need come from further importations of gold in settlement of our heavy trade balances, provided proper methods are employed to control the gold and to prevent undue expansion. The consensus of opinion was that a general adherence to a policy of prudence and conservatism would be the surest means of maintaining our present prosperous conditions.

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

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November 24, 1916.

Dear Sir:

The Federal Reserve Board has observed that certain Federal reserve banks have recently purchased two per cent United States bonds above par and its attention has been directed to the fact that this price has been artificially stimulated by the competitive bidding of those Federal reserve banks.

While it is not the desire of the Board to restrict or to limit the purchase of two per cent bonds by the various Federal reserve banks, it is deemed advisable to point out that this policy, which is unnaturally forcing up the price of two per cent bonds, is fraught with certain dangers.

Section 18 of the Federal Reserve Act provides in part that 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 Federal Reserve Board is given the power to require Federal reserve banks to buy $25,000,000 of such bonds in any one year, less the amount of bonds bought by such Federal reserve banks in the open market during the same calendar year. The power of the Federal reserve banks to make open market purchases of bonds is not limited by law, so that, strictly speaking, such banks are acting within their legal rights in making such purchases even though their competitive bidding is forcing the price of two's above par.

The difficulty, however, is that this policy is creating an artificial and unnatural market for two per cent bonds. The Federal reserve banks are afforded the privilege of converting a certain amount of two per cent bonds into three per cent bonds and three per cent one-year notes. Consequently, such banks will not suffer any direct financial loss by paying for two per cent bonds practically the same amount as the normal market price for three per cent bonds. The fact, however, that Federal reserve banks may convert bonds in this manner and that two per cent bonds are because of the conversion privilege worth substantially as much as three's to Federal reserve banks, is hardly a sound reason to justify their forcing of the price of two's above their normal market value by blindly bidding against one another.

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It is quite generally agreed that one of the purposes of the Act was to promote a gradual retirement of the national bank circulation, and Section 18 in affording a fixed market, at par and accrued interest, for two per cent bonds against which circulation is outstanding, contemplated that member banks would dispose in that manner of those bonds which they are required by the national bank act to keep on deposit with the Treasurer of the United States.

It is apparent, therefore, that if the open market price of two per cent bonds is unnaturally established at a figure above par, member banks will not be inclined to offer their two per cent bonds for sale through the Treasurer at par and accrued interest, even if such bonds are not free bonds and can not be released by the Treasurer for sale in any manner other than that provided by Section 18. The result will be that there will be an artificial stoppage of the retirement of national bank circulation in the manner contemplated by the Act.

The suggestion has been made that the Federal reserve banks appoint a committee to consider the purchase of two per cent bonds for the joint account of all Federal reserve banks. The Board believes that such a course would not only be conducive to a more healthy and normal market for two per cent bonds, but also that it would best promote the results intended by Congress in the matter of accomplishing the retirement of national bank circulation.

Respectfully,

Governor.

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Estimated gold stock of the country June 30, 1914 and 1916, compared with total loans and discounts of all banks and trust companies in the United States on the same dates.

(In thousands of dollars)

	June 30, 1914.	June 30, 1916.
Estimated stock of gold of country	1,891	2,440
Loans and discounts of all banks and trust companies	15,340	17,850
Per cent of gold stock to loans and discounts	12.3%	13.7%
Each dollar of gold supported the following amounts of loans and discounts	$8.11	$7.32

Respectfully submitted,

M. JACOBSON,

November 21, 1916.

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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 24, 1916.

Dear Sir:

You have probably seen the brief statement which was given to the press in regard to the meeting of the Advisory Council which was held here on the 20th and 21st instants. It seems proper however to write you more fully regarding the most important topic that was considered at the meeting, in order that your directors may be better advised as to the views of the Federal Advisory Council and of the Federal Reserve Board regarding the regulation and control of our gold supply and the extension of credits to foreign countries. Neither the Council nor the Board entertains the opinion that has been recently expressed by some financiers that a further addition to the stock of gold in this country would be, of itself and necessarily, a danger which we should seek to avoid by having our banking funds absorbed by extensive operations in foreign government obligations, whether of short or long maturity. The difficulties and evils which might in time develop out of such a policy would be far more serious than any situation which may arise in connection with the effective handling of continuing accessions of gold, even though these should attain a larger volume than they have thus far. There are several means which could be employed to counteract any inflationary tendencies or distrubing effects that might result from a further increase in our gold supply. One that was suggested is an amendment to the law giving authority to the Federal Reserve Board to make the reserve provisions which will become operative under the law as it now stands on November 16, 1917, effective at any time prior to

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that date upon sixty days notice to member banks, and the Council by unanimous vote went on record as favoring such an amendment. This recommendation contemplates the discontinuance at an early date of the practice of counting balances with approved reserve agents as reserves, and the consequent restriction of legal reserves to balances with Federal Reserve Banks and lawful money in the vaults of member banks. The Federal Advisory Council expressed the opinion, in which the Board concurs, that this change could be effected now or in the near future without inconvenience and to the real benefit of the country, and that it would be highly desirable to make it at a time when it can be done without any shock and when the increase of real reserves with the Federal Reserve Banks would be so effective in strengthening the control of the country's gold supply and would at the same time minimize any apprehensions that might be felt because of its increasing volume. We cannot tell what conditions will be in November 1917, but we do know that the wiping out of $200,000,000 of fictitious reserves, which would be the result of treating the $600,000,000 of bank deposits held by banks in reserve and central reserve cities as bank balances only, could be effected at the present time without any disturbance, and that such a course would have a sobering effect.

The Council concurred in the opinion which was a short time ago adopted by the Board, and went even further, in asserting that acceptances made with an agreement on the part of the accepting banks for a series of renewals, while technically eligible for purchase by Federal Reserve Banks, are in no sense self-liquidating within the time fixed by law and cannot be regarded as strictly instruments of credit such as are based on commercial transactions which in themselves provide for their retirement at maturity, and recommended that the purchase of them by the Federal Reserve Banks

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should be made in moderate amounts only, if not discouraged altogether. Some members of the Council called attention to the fact that in some financial centers bank reserves are already down close to the legal requirements and that there is a possibility of an advance in discount rates in the not distant future; while others reported that in some localities there is noticeable a tendency on the part of member banks toward overinvestment in local and foreign obligations. The Board and the Council are a unit in agreeing that it is very important at this time for our banking institutions to keep themselves in a strong position and to maintain as far as possible the liquidity of their assets. A general policy of prudence and conservatism was recommended by the Council, and the Board feels that the Federal Reserve Banks cannot urge such a course too strongly upon their member banks.

The foregoing is not for publication and any suggestions based thereon should be made with discretion.

Very truly yours,

Governor.

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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 690.
H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 27, 1916.

To the Federal Reserve Board,

Washington.

Gentlemen:

On May 10, 1916, I prepared for the Board a short statement dealing with Governor Hamlin's brief on the subject of note issue amendments. I took the position at that time that there were three amendments to the Federal Reserve Act relating to this matter which were very desirable:

(1) The right to issue Federal Reserve notes directly for gold;

(2) A consolidation or combination of the accounts of the Federal Reserve Agents and the Federal Reserve Banks so that we would have the responsibility of the Banks behind the custody of the notes, and not only that of the Federal Reserve Agent, so as to provide that the Reserve Banks shall show all notes outstanding in the hands of the public as a liability and all assets held against them as an asset of the Bank;

(3) An amendment to Section 14, of the Federal Reserve Act which would liberalize the law in respect to collateral behind Federal Reserve notes by making eligible as collateral bankers' acceptances, or what is known as "bought paper", as well as commercial paper rediscounted for member banks.

I then took the position that if these three amendments were secured it would be neither necessary nor desirable to ask Congress to make Federal Reserve notes legal reserve.

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Since that memorandum was written the third of the above mentioned amendments has been passed by Congress and another amendment has also been passed which has a very important bearing on the situation, to-wit: the authority to member banks to keep any part of their reserve with the Federal Reserve Bank, instead of in their own vaults. I still believe that the amendments suggested by me on May 10th are very desirable and that if they were passed it would not be necessary, at least at this time, to make Federal Reserve notes available as bank reserves. However, the proposal, so ably urged by my colleague, Mr. Warburg, is entitled to the most careful consideration, first, as to the desirability of the object sought, and, second, as to whether there is any better means of attaining it.

First, as to the object sought. It appears to be Mr. Warburg's desire to impound in the Federal Reserve Banks a very large share of the country's gold supply, whereas I rather question the desirability of going too far in that direction. My feeling is that, under the changes in the law which I have suggested, we would have little difficulty in accumulating in the Federal Reserve Banks half of the gold stock of the country not in the hands of the Federal Government. If the other half were in the hands of the public and in those of member and non-member banks it would be where it could serve an important purpose as a sort of secondary reserve supply which would be called upon in case of great need. If our banking system was

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under a strong central management, and the form of our Government was like that of the German Empire, I can readily see where it would be natural and perhaps desirable to act on Mr. Warburg's suggestion, but, considering the form of our Government, the temperament of our people, and the dangers of over-expansion and over-speculation, I think we should not put all of our golden eggs in one basket.

We all recall that the panic of 1907 came as a climax to several years of great expansion in expenditures in all kinds of business enterprises, a period of ten or eleven years of pyramiding upwards almost without interruption. Six months before the panic came many wise men thought that things looked "squally", and yet the temptation to keep on stretching bank resources to the limit was too strong even for them to resist. For this and other reasons I can not help feeling that there is danger in putting all the elasticity in the Federal Reserve Banks and not leaving a reserve of elasticity in the banks of the country. Of course, I am aware it is somewhat inconsistent to say that a balance with the Reserve Bank shall be counted as a reserve, whereas, the notes of the Bank can not be so counted. I am also aware of the fact that as time goes on bank balances are going to play a greater part than Federal Reserve notes; that when our check clearing and collection plan is fully developed, member banks will care less about drawing out Federal Reserve notes, and more about transferring balances by drafts and

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checks, On the other hand, the use of Federal Reserve notes will be always greatest in the parts of the country where there is the greatest necessity for caution; in those parts of the country where other credit instruments play a smaller part and where actual currency plays a larger part.

I can see that if we do not make Federal Reserve notes reserve and if we permit, say one-half of the gold holdings of the country to remain in the hands of member and non-member banks, we may sometimes reach a point where a Federal Reserve Bank has exhausted its unpledged gold supply and can not issue any more notes. Member banks, coming to their Federal Reserve Bank to borrow will, in such a case, complain that "the well has run dry", but when that time comes the Federal Reserve Bank will say to those member banks, "If you have gold in your reserves and will deposit it with us we can help you, because we can immediately expand that gold in the ratio of 1.625 to 1, and we can hold your gold to count as reserve and still help you with currency or book credits."

I agree entirely with Mr. Warburg's argument that we should put ourselves in a position to release gold freely when the European war is over. For us, as a nation to have accumulated through a favorable trade balance an enormous fund of gold and then attempt to put the bars up and so prevent the world's supply of gold from seeking its natural level would be absurd and even monstrous.

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Such action on our part might very properly lead to a demonetization of gold, but I can not conceive that gold will go out of the country except in four ways; first, by a reversal in the balance trade; second, by the spending of money in Europe by Americans; third, by remittances to Europeans by Americans and immigrants; fourth; by loans to Europe.

There are some other general reasons against making Federal Reserve notes reserve which might also be mentioned. It is bad education for the public to let it imagine that a note of a bank is reserve because Congress says it is reserve. The fundamental reliance of our whole structure is the gold, or metallic basis behind our currency. While it is true that the Government guarantees the notes, every one of us will take the position that the notes must be secure, without leaning upon the Government and without even suggesting that the Government shall ever be called upon to make them good. The Government supervises their issue, must be satisfied that the security and the reserve behind them is ample and sufficient, but it was never seriously meant that the Government was going to tax the people to pay these notes.

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Viewed from this aspect, it isn't good economics for Congress to say that "greenbacks", or any other kind of notes that are not based on the deposit of 100% of gold can be called the ultimate reserve of member banks. The fact that we have taken some wrong steps in this direction in the past does not at all justify our doing it again. The greenback is simply the promise of the Government with a gold security of approximately 35%; the national bank note besides being the obligation of the issuing bank is security of the Government, as attested by the deposit of the United States bonds and has a gold reserve of only 5%. The Federal Reserve note has 100% of commercial paper as collateral, and 40% or more of gold reserve behind it, besides which it has the guarantee of the Federal Reserve Banks, the member banks, and the Government. No one of these three kinds of currency can properly be considered ultimate reserves, and they are unquestionably good and ought to be in every sense legal tender. It appears inconceivable that they should not be absolutely good at all times and readily acceptable by the people in all sorts of transactions as a substitute for actual specie. When it comes to

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international transactions, gold, or its equivalent only, can be used, but in all intra-national transactions there is no reason why these various representatives of money should not perform all the functions, except those of being ultimate reserves. The fact that state banks are permitted to use national bank notes and reserve notes as reserves and a actually do so, only accentuates the necessity of keeping the ultimate reserves inviolable.

The object which Mr. Warburg seeks to attain - of securing a much larger share of the ultimate reserves of the country in the hands of the Federal Reserve Banks - might be attained in another and possibly less dangerous way if the Federal Reserve Act were so amended as to state only those reserves which member banks must carry with their Federal Reserve Bank, stating in so many words that the specie and currency which any bank shall carry in its own vault, or till, will be left to its own judgment. The ultimate reserves, in other words, will be with the Federal Reserve Bank. The advantage of this method to the member bank would be that the many kinds of currency in its possession, as well as specie, would serve its purpose equally well - gold or silver certificates, greenbacks, national

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bank note currency, Federal Reserve notes, or Federal Reserve Bank notes. What the reserves should be is necessarily a matter of study and calculation, but suppose, for example, we should start out with the proposal that country bank reserves held with the Federal Reserve Bank should be 8%, the member banks in reserve cities should hold 12%, and the member banks in central reserve cities should hold 15%. In this connection it is proper to mention that under the laws of a number of states the required cash reserves is left entirely in the judgment of the banker, and in European countries it is the custom to let bankers use their own discretion as to the cash reserves they shall hold. While it is not suggested that this discretion apply to the entire reserves, it is thought that it can be safely applied to the bank's own counter cash and vault requirements.

This may not be the best solution of the problem, yet it is at least worthy of consideration. If, on the other hand, Mr. Warburg's plan is adopted, he, himself, admits that it would be desirable to keep, not 40% of gold behind Federal Reserve notes, but 60% or 70%. Indeed, it is probable that it would be necessary to change the law in regard to ultimate or gold reserve behind Federal Reserve notes and to raise the limit below which a penalty, or tax, shall apply to, say 50%.

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There are other ways in which, without any Congressional action, much might be accomplished to put the gold of the country in the hands of the Federal Reserve Banks and member banks, rather than by leaving it where it will be hoarded by people, or used for every-day currency; that is, by readjusting the denominations of gold and silver certificates and other forms of currency. As it has been pointed out several times, if gold certificates were not printed in denominations less than $50, gold certificates would rarely appear as currency, and become, as they should be, almost exclusively reserve money.

From the above, it will appear that, while I am not favorable to the plan of making Federal Reserve notes reserve, I am not opposed to a limited extent, at least to the object Mr. Warburg has in view, to wit: the greater concentration of gold in Reserve Banks.

Respectfully submitted,

F. A. DELANO.

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STATEMENT FOR THE PRESS.

November 27, 1916.

The Federal Reserve Board today made public the following statement relating to foreign credits, which is to appear in the next issue of the Federal Reserve Bulletin:

In view of contradictory reports which have appeared in the press regarding its attitude toward the purchasing by banks in this country of Treasury bills of foreign governments, the Board deems it a duty to define its position clearly. In making this statement the Board desires to disclaim any intention of discussing the finances or of reflecting upon the financial stability of any nation, but wishes it understood that it seeks to deal only with general principles which affect all alike.

The Board does not share the view frequently expressed of late, that further importations of large amounts of gold must of necessity prove a source of danger or disturbance to this country. That danger, the Board believes, will arise only in case the inflowing gold should remain uncontrolled and be permitted to become the basis of undesirable loan expansions and of inflation. There are means, however, of controlling accessions of gold by proper and voluntary cooperation of the banks or if need be by legislative enactment. An important step in this

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direction would be the anticipation of the final transfer of reserves contemplated by the Federal Reserve Act to become effective on November 16, 1917. This date could be advanced to February or March 1917. Member banks would then be placed on the permanent basis of their reserve requirements and fictitious reserves would then disappear and the banks have a clearer conception of actual reserve and financial conditions. It will then appear that while a large increase in the country's gold holdings has taken place the expansion of loans and deposits has been such that there will not remain any excess of reserves, apart from the important reserve loaning power of the Federal Reserve banks.

In these circumstances the Board feels that member banks should pursue a policy of keeping themselves liquid; of not loaning down to the legal limit, but of maintaining an excess of reserves - not with reserve agents, where their balances are loaned out and constitute no actual reserve, but in their own vaults or preferably with their Federal Reserve banks. The Board believes that at this time banks should proceed with much caution in locking up their funds in long term obligations or in investments, which are short term in form or name but which, either by contract or through force of circumstances, may in the aggregate have to be renewed until normal condi-

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tions return. The Board does not undertake to forecast probabilities or to specify circumstances which may become important factors in determining future conditions. Its concern and responsibility lies primarily with the banking situation. If, however, our banking institutions have to intervene because foreign securities are offered faster than they can be absorbed by investors - that is their depositors - an element would be introduced into the situation which, if not kept under control, would tend toward instability, and ultimate injury to the economic development of this country. The natural absorbing power of the investment market supplies an important regulator of the volume of our sales to foreign countries in excess of the goods that they send us. The form which the most recent borrowing is taking, apart from reference to its intrinsic merits, makes it appear particularly attractive as a banking investment. The Board, as a matter of fact, understands that it is expected to place it primarily with banks. In fact it would appear so attractive that unless a broader and national point of view be adopted, individual banks might easily be tempted to invest in it to such an extent that the banking resources of this country employed in this manner might run into many hundreds of millions of dollares. While the loans may be short in form and severally, may be collected at maturity, the object of the borrower must be to attempt

to renew

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them collectively, with the result that the aggregate amount placed here will remain until such time as it may be advantageously converted into a long term obligation. It would, therefore, seem as a consequence that liquid funds of our banks, which should be available for short credit facilities to our merchants, manufacturers and farmers, would be exposed to the danger of being absorbed for other purposes to a disproportionate degree, especially in view of the fact that many of our banks and trust companies are already carrying substantial amounts of foreign obligations, and of acceptances which they are under agreement to renew. The Board deems it therefore, its duty to caution the member banks that it does not regard it in the interest of the country at this time that they invest in foreign Treasury bills of this character.

The Board does not consider that it is called upon to advise private investors, but as the United States is fast becoming the banker of foreign countries in all parts of the world, it takes occasion to suggest that the investor should receive full and authoritative data - particularly in the case of unsecured loans - in order that he may judge the future intelligently in the light of present conditions and in conjunction with the economic developments of the past.

The united States has now attained a position of wealth and of international financial power, which, in the natural course

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of events, it could not have reached for a generation. We must be careful not to impair this position of strength and independence. While it is true that a slowing down in the process of credit extension may mean some curtailment of our abnormally stimulated export trade to certain countries we need not fear that our business will fall off precipitately should we become more conservative in the matter of investing in loans, because there are still hundreds of millions of our own and foreign securities held abroad which our investors would be glad to take over, and moreover, trade can be stimulated in other directions.

In the opinion of the Board, it is the duty of our banks to remain liquid in order that they may be able to continue to respond to our home requirements, the nature and scope of which none can foresee, and in order that our present economic and financial strength may be maintained when, at the end of the war we shall wish to do our full share in the work of international reconstruction and development which will then lie ahead of us, and when a clearer understanding of economic conditions as they will then exist, will enable this country more safely and intelligently to do its proper part in the financial rehabilitation of the world.

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1654

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

595.

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 28, 1916.

Dear Sir:

It has been recently brought to the attention of the Federal Reserve Board that in certain instances an officer or employee of the Federal Reserve Bank serves also as Assistant to the Chairman and Federal Reserve Agent at that Bank. The continuance of this relationship has been discussed by the Board and the conclusion reached that it is inadvisable. It was, therefore, voted by the Board on November 25, 1916, that such joint employment should not be permitted in the future and that in cases where it now exists the relationship should be terminated on December 31, 1916.

Will you please take the steps necessary in this matter and advise the Board of the action taken.

Very truly yours,

Secretary.

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

897

December 6, 1916.

Dear Sir:

There is inclosed for your information and attention copy of a resolution adopted by the Federal Reserve Board at a meeting held on December 5, levying an assessment of one-tenth of one per cent (.001) against Federal Reserve Banks to defray the estimated general expenses of the Federal Reserve Board from January 1 to June 30, 1917. This assessment does not include the cost of engraving and printing Federal reserve notes.

There is also inclosed a statement showing the basis upon which the assessment is levied.

I have the honor to request that you bring this matter to the early attention of the Board of Directors of your bank, and forward the assessment to the Federal Reserve Board, one-half to be payable January 1st, and one-half on March 1, 1917, as indicated in the resolution.

Very truly yours,

Fiscal Agent.

Inclosures.

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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 semiannually 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 employes for the half year succeeding the levying of such assessment, together with any deficit carried forward from the preceding half year; and

WHEREAS, it appears from estimates submitted and considered that it is necessary that a fund equal to one-tenth of one per cent (.001) of the capital stock of the Federal Reserve Banks be created for the purposes hereinbefore described, exclusive of the cost of engraving and printing Federal reserve notes;

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 one-tenth of one per cent (.001) of the total capital stock of such banks, and the fiscal agent of the Board is hereby authorized to collect from said banks such assessment and execute, in the name of this Board, a receipt for payment made. Such assessment will be collected in two instalments of one-half each; the first instalment to be paid on January 1, 1917, and the second half on March 1, 1917.

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ESTIMATE FOR JANUARY ASSESSMENT, 1917.

	COMMITMENTS				
	July 1 to Nov. 30 1916	Estimated for December 1916	TOTAL	Monthly Average	Estimated Average Monthly requirement January 1 to June 30 1917
PERSONAL SERVICES:					
Board and its clerks	$36,925.02	$ 7,375.04	$44,300.06	$ 7,383.34	$ 7,375.04
Secretary's Office	11,048.33	2,595.01	13,643.34	2,273.89	2,595.01
Counsel's Office	10,333.32	2,066.66	12,399.98	2,066.66	2,066.66
Division of Audit & Examination	6,691.67	1,338.34	8,030.01	1,338.33	1,438.34
Division of Reports & Statistics	4,454.16	1,030.00	5,484.16	914.03	1,030.00
Division of Issue	3,454.34	648.34	4,102.68	683.78	718.34
Messengers	1,760.00	365.00	2,125.00	354.17	365.00
Charwomen	296.00	60.00	356.00	59.33	60.00
	$74,962.84	$15,478.39	$90,441.23	$15,073.53	$15,648.39
NON-PERSONAL SERVICES:					
Transportation & Subsistence of Persons:					
Board and its clerks	$ 600.63	$ 100.00	$ 760.63	$ 126.77	$ 100.00
Secretary's Office	25.05	--- --	25.05	4.17	10.00
Division of Audit & Exaination	2,719.88	300.00	3,019.88	503.33	625.00
Division of Reports & Statistics	19.20	--- --	19.20	3.20	--- --
Counsel's Office	--- --	--- --	--- --	--- --	10.00
Messengers (Carfare)	15.00	--- --	15.00	2.50	3.00

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COMMUNICATION SERVICE:					
Telephone	$ 301.58	$ 60.00	$ 361.58	$ 60.26	$ 60.00
Telegraph	1,743.72	300.00	2,043.72	340.62	333.00
Postage	20.00	--- --	20.00	3.33	5.00
PRINTING, BINDI[illegible] etc.	5,416.83	2,700.00	8,116.83	1,352.80	1,250.00
CONTRACT REPAIRS	40.34	--- --	40.34	6.72	10.00
ELECTRICITY (Light & Power)	150.00	30.00	180.00	30.00	30.00
STEAM (Heat)	15.00	15.00	30.00	5.00	15.00
OTHER (Non-personal services)	173.98	10.00	183.98	30.66	50.00
SUPPLIES:					
Stationery	569.94	150.00	719.94	119.99	125.00
Periodicals	145.90	--- --	145.90	24.32	20.00
Other	109.71	25.00	134.71	22.45	40.00
EQUIPMENT:					
Furniture & Office Equipment	1,480.75	200.00	1,680.75	280.13	150.00
Books	111.15	--- --	111.15	18.53	25.00
CONTINGENCIES	--- --	--- --	--- --	--- --	650.00
	$88,681.50	$19,368.39	$108,049.89	$18,008.31	$19,159.39

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1701

ESTIMATE FOR JANUARY 1917 ASSESSMENT.

Average monthly encumbrance for period July 1, 1916, to December 31, 1916..... $18,008.31

Estimated monthly requirements - January to June, inclusive, 1917..... 19,159.39

Estimated monthly increase..... $ 1,151.08

* * * * * * * * * * *

Estimated requirements - January to June, inclusive, 1917.....$114,956.34

Estimated unencumbered balance January 1, 1917..... 10,099.36

$104,856.98

* * * * * * * * * * *

Total capitalization Federal Reserve Banks - December 1, 1916.....$111,474.000.

Rate of assessment to produce $111,474.00..... (1/10 of 1%).....001

Approved: Committee on Organization Expenditures & Staff.

F. A. DELANO)
C. S. HAMLIN)
A. C. MILLER)

SHERMAN ALLEN.
Fiscal Agent.

December 5, 1916.

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1702

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

898
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

December 6, 1916.

Dear Sir:

In preparing volumes of the Federal Reserve Bulletin for 1916 for binding, the Federal Reserve Board finds that it has but few copies of the issue of January, 1916. If you have copies of this number which you can contribute to the Board's supply it will greatly appreciate your forwarding them under the inclosed frank.

The cost of binding Federal Reserve Bulletins for the year 1915 at the Government Printing Office was about $ 1.00 per volume. If you desire to forward not to exceed six sets of Bulletins to be bound and returned to you, the Board will have the binding done in connection with its order, charging you the pro rata expense. In order to distinguish Bulletins sent for binding and those contributed to the Board's supply, please mark those for binding both inside and outside the package and advise the Board by letter of the number of sets which you desire to have bound.

Very truly yours,

Secretary.

Inclosure.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 19 of the Act approved December 23, 1913, amended by an Act of August 14, 1914, be further amended and re-enacted so as to read as follows:

Sec. 19. 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 deposit which are subject to not less than thirty days' notice before payment, AND ALL POSTAL SAVINGS DEPOSITS.

~~When the Secretary of the Treasury shall have officially announced, in such manner as he may elect, the establishment of a Federal reserve bank in any district, every subscribing member~~ EVERY bank, BANKING ASSOCIATION, OR TRUST COMPANY WHICH IS OR WHICH BECOMES A MEMBER OF ANY FEDERAL RESERVE BANK shall establish and maintain BALANCES WITH ITS FEDERAL RESERVE BANK ~~reserves~~ as follows:

(a) A bank not in a reserve or central reserve city as now or hereafter defined shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT A BALANCE IN COLLECTED AVAILABLE FUNDS ~~reserves~~ equal to NOT LESS THAN ~~twelve~~ SEVEN per centum of the aggregate amount of its demand deposits and ~~five~~ THREE per centum of its time deposits, ~~as follows:~~

~~In its vaults for a period of thirty six months after said date five-twelfths thereof and permanently thereafter four-twelfths.~~

~~In the Federal reserve bank of its district, for a period of twelve months after said date, two-twelfths, and for each succeeding six months an additional one-twelfth, until five-twelfths have been so deposited, which shall be the amount permanently required.~~

~~For a period of thirty-six months after said date the balance of the reserve may be held in its own vaults, or in the Federal reserve bank, or in national banks in reserve or central reserve cities as now defined by law.~~

~~After said thirty-six months' period, said reserves, other than those hereinbefore required to be held in the vaults of the member bank and in the Federal reserve bank, shall be held in the vaults of the member bank or in the Federal reserve bank or in both, at the option of the member bank.~~

(b) A bank in a reserve city, as now or hereafter defined, shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT A BALANCE IN COLLECTED AVAILABLE FUNDS ~~reserves~~ equal to NOT LESS THAN ~~fifteen~~ TEN per centum of the aggregate amount of its demand deposits and ~~five~~ THREE PER centum of its time deposits, ~~as follows:~~

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~~In its vaults for a period of thirty-six months after said date six-fifteenths thereof, and permanently thereafter five-fifteenths.~~

~~In the Federal reserve bank of its district for a period of twelve months after the date aforesaid at least three-fifteenths, and for each succeeding six months an additional one-fifteenth, until six-fifteenths have been so deposited, which shall be the amount permanently required.~~

~~For a period of thirty-six months after said date the balance of the reserves may be held in its own vaults, or in the Federal reserve bank, or in national banks in reserve or central reserve cities as now defined by law.~~

~~After said thirty-six months' period all of said reserves except those hereinbefore required to be held permanently in the vaults of the member bank and in the Federal reserve bank, shall be held in the vaults or in the Federal reserve bank, or in both, at the option of the member bank.~~

(c) A bank in a central reserve city, as now or hereafter defined, shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT a BALANCE IN COLLECTED AVAILABLE FUNDS ~~reserve~~ equal to NOT LESS THAN ~~eighteen~~ THIRTEEN per centum of the aggregate amount of its demand deposits and ~~five~~ THREE per centum of its time deposits ~~as follows:~~

~~In its vaults six-eighteenths thereof.~~
~~In the Federal reserve bank seven-eighteenths.~~
~~The balance of said reserves shall be held in its own vaults or in the Federal reserve bank at its option.~~

~~Any Federal reserve bank may receive from the member banks as reserves, not exceeding one-half of each installment, eligible paper as described in section fourteen, properly indorsed and acceptable to the said reserve bank.~~

~~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~~ No member bank shall keep on deposit with any nonmember bank a sum

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in excess of ten per centum of its own paid-up capital and surplus UNLESS SAID NONMEMBER BANK SAHLL HAVE QUALIFIED AS AN ASSOCIATE MEMBER BANK UNDER THE PROVISIONS OF SECTION _____ OF THIS ACT. No member bank shall act as a medium or agent of a nonmember 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~~, UNLESS SAID NONMEMBER BANK SHALL HAVE QUALIFIED AS AN ASSOCIATE MEMBER UNDER THE PROVISIONS OF SECTION OF THIS ACT.

The REQUIRED BALANCE ~~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~~ BALANCE required by law is fully restored.

In estimating the ~~reserves~~ BALANCES required by this Act, the net DIFFERENCE ~~balance~~ of amounts due to and from other banks shall be taken as the basis for ascertaining the deposits against which ~~reserves~~ REQUIRED BALANCES WITH FEDERAL RESERVE BANKS shall be determined. ~~Balances in reserve banks due to member banks shall to the extent herein provided, be counted as reserves.~~

National banks OR BANKS ORGANIZED UNDER LOCAL LAWS located in Alaska or outside the continental United States may remain nonmember banks, and shall in that event maintain reserves and comply with all the conditions now provided by law regulating them; or said banks ~~except in the Philippine Islands~~, may, with the consent of the Federal Reserve Board become member banks of any one of the reserve districts, and shall, in that event, take stock, maintain reserves and be subject to all the other provisions of this Act.

THIS ACT SHALL BECOME EFFECTIVE SIXTY DAYS AFTER ITS PASSAGE.

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AMENDMENT TO SECTION 22.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That that part of Section 22 of the Act approved December 23, 1913, known as the Federal Reserve Act, which reads as follows:

> "Other than the usual salary or director's fees 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,"

be and hereby is amended and re-enacted so as to read as follows:

> Other than the usual salary or director's ~~fees~~ FEE paid to any officer, director, ~~or~~ employee OR ATTORNEY of a member bank and other than a reasonable fee paid by said bank to such officer, director, ~~or~~ employee, OR ATTORNEY 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, PROVIDED, HOWEVER, THAT NOTHING IN THIS ACT CONTAINED SHALL BE CONSTRUED TO PROHIBIT A DIRECTOR, OFFICER, OR EMPLOYEE FROM RECEIVING THE SAME RATE OF INTEREST PAID TO OTHER DEPOSITORS FOR SIMILAR DEPOSITS MADE WITH SUCH BANK, OR TO PROHIBIT A DIRECTOR, WHO IS NOT AN OFFICER, OR EMPLOYEE, FROM RECEIVING, DIRECTLY OR INDIRECTLY, THE USUAL AND CUSTOMARY COMMISSIONS OR FEES FOR SERVICES RENDERED IN BUYING AND SELLING SECURITIES OR OTHER INVESTMENTS FOR OR ON ACCOUNT OF SUCH BANK, BUT IN THIS LATTER CASE THE ACTION OF THE BOARD OF DIRECTORS, IN DIRECTING THE PURCHASE OR SALE OF SUCH SECURITIES OR OTHER INVESTMENTS, MUST BE RECORDED IN THE MINUTES OF THE MEETING OF SAID BOARD, AND SUCH MINUTES MUST SPECIFY THE NAME OF THE DIRECTOR, OFFICER, OR EMPLOYEE AND THE FIRM OR CORPORATION WITH WHICH HE IS CONNECTED, IF ANY, THROUGH WHICH SUCH ORDER IS TO BE EXECUTED, AND, PROVIDED, FURTHER, THAT NOTES, DRAFTS, BILLS OF EXCHANGE OR OTHER EVIDENCES OF DEBT EXECUTED OR INDORSED BY DIRECTORS OF A MEMBER BANK MAY BE DISCOUNTED WITH SUCH MEMBER BANK ON THE SAME TERMS AND CONDITIONS AS OTHER NOTES, DRAFTS, BILLS OF EXCHANGE OR EVIDENCESOF DEBT UPON THE AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS THE MEMBERS OF THE BOARD OF DIRECTORS OF SUCH MEMBER BANK.

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AMENDMENT TO SECTION 22.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATESOF AMERICA IN CONGRESS ASSEMBLED, That that part of Section 22 of the Act approved December 23, 1913, known as the Federal Reserve Act, which reads as follows:

> "Other than the usual salary or director's fees 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 business of the bank,"

be and hereby is amended and re-enacted so as to read as follows:

> "Other than the usual salary or director's ~~fees~~ FEE paid to any officer, director, or employee OR ATTORNEY of a member bank and other than a reasonable fee paid by said bank to such officer, director, or employee, OR ATTORNEY 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, PROVIDED, HOWEVER, THAT NOTHING IN THIS ACT CONTAINED SHALL BE CONSTRUED TO PROHIBIT A DIRECTOR, OFFICER, OR EMPLOYEE FROM RECEIVING THE SAME RATE OF INTEREST PAID TO OTHER DEPOSITORS FOR SIMILAR DEPOSITS MADE WITH SUCH BANK; OR TO PROHIBIT A DIRECTOR, WHO IS NOT AN OFFICER OR EMPLOYEE, FROM RECEIVING, DIRECTLY OR INDIRECTLY, THE USUAL AND CUSTOMARY COMMISSIONS OR FEES FOR SERVICES RENDERED IN BUYING AND SELLING SECURITIES OR OTHER INVESTMENTS FOR OR ON ACCOUNT OF SUCH BANK, BUT IN THIS LATTER CASE THE ACTION OF THE BOARD OF DIRECTORS, IN DIRECTING EACH PURCHASE OR SALE OF SUCH SECURITIES OR OTHER INVESTMENTS, MUST BE BY AN AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD EXCLUSIVE OF THE DIRECTOR INTERESTED, AND MUST BE RECORDED IN THE MINUTES OF THE MEETING OF SAID BOARD, SUCH MINUTES TO SPECIFY THE NAME OF THE DIRECTOR AND THE FIRM OR CORPORATION WITH WHICH HE IS CONNECTED, IF ANY, THROUGH WHICH SUCH ORDER IS TO BE EXECUTED TOGETHER WITH THE AMOUNT OF THE FEE OR COMMISSION TO BE PAID ON EACH TRANSACTION; AND, PROVIDED, FURTHER, THAT NOTES, DRAFTS, BILLS OF EXCHANGE OR OTHER EVIDENCES OF DEBT EXECUTED OR INDORSED BY DIRECTORS OF A MEMBER BANK MAY BE DISCOUNTED WITH SUCH MEMBER BANK ON THE SAME TERMS AND CONDITIONS AS OTHER NOTES, DRAFTS, BILLS OF EXCHANGE OR EVIDENCES OF DEBT UPON THE AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD OF DIRECTORS OF SUCH MEMBER BANK.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 11 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act approved September 7, 1916, be and is hereby amended by adding at the end thereof two new clauses as follows:

(n) Upon the request of a Federal reserve bank to authorize it from time to time to repay to its member banks a part of their cash-paid subscriptions to its capital stock, provided, however, that such cash-paid subscriptions shall never be less than one and one-half per centum of the paid-up capital stock and surplus of the respective member banks and shall be the same percentage for every member bank in any one district, and provided, further, that the subscribed capital stock of Federal reserve banks and the liability of stockholders shall remain as now provided by law. Nothing herein contained shall be construed to deny the right of the Federal Reserve Board, in its discretion, to call the balance, or any part thereof, of any member bank's subscription to the capital stock of its Federal reserve bank.

All provisions of law inconsistent with any of the provisions of this clause are to that extent and to that extent only hereby repealed.

(o) Whenever extraordinary conditions justify, to increase, from time to time for periods not exceeding ------ days, on the affirmative vote of five of its members, the amount of balances required by this Act to be maintained by member banks with their respective Federal reserve banks, provided, such increase shall at no time exceed ----- per centum of such required balances, and provided, further, that the Federal Reserve Board shall make a report to Congress in writing setting forth the conditions on which such action is based.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 11 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act approved September 7, 1916, be and is hereby amended by adding at the end thereof a new clause as follows:

(n) Whenever extraordinary conditions justify, to increase, from time to time for periods not exceeding - - - days, on the affirmative vote of five of its members, the amount of balances required by this Act to be maintained by member banks with their respective Federal reserve banks, provided, such increase shall at no time exceed - - - per centum of such required balances, and provided, further, that the Federal Reserve Board shall make a report to Congress in writing setting forth the conditions on which such action is based.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED,

That every national banking association possessing a capital of more than one hundred and fifty thousand dollars shall pay to the Treasury of the United States in the months of January and July, in addition to the tax now imposed by existing law, a tax of per centum each half year upon the average amount of its notes in circulation in excess of eighty per centum of its capital, Provided, that after January, 1918, the tax thus imposed shall apply to the average amount of its notes in circulation in excess of sixty-five per centum of its capital, and after January, 1919, the tax thus imposed shall apply to the average amount of its notes in circulation in excess of fifty per centum of its capital, Provided, however, that the tax imposed by this Act shall in no event be construed to apply to the circulating notes of a bank which are not in excess of one hundred and fifty thousand dollars.

The first payment of the tax imposed by this Act shall not be due until July, 1917, and shall be at the rate of per centum per annum and shall be based on the average circulation outstanding, during the period between a date thirty days after the passage of this Act and the date of the payment of the tax in July, 1917.

No national banking association hereafter organized, regardless of the amount of its capital stock shall be permitted to issue circulating notes in excess of fifty per centum of its capital stock.

So much of the provisions of Section nine of the Act of March 4, 1907, as limits the deposit of lawful money with the Treasurer of the United States for the purpose of withdrawing national bank circulation to nine million of dollars in any one month shall not be construed to apply to the deposit of lawful money made for the purpose of wiehdrawing circulation which is subject to the tax imposed by this Act.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 5202 of the Revised Statutes of the United States, as amended by Section 13 of the Act approved December 23, 1913, known as the Federal Reserve Act, as further amended by the Act approved September 7, 1916, be and is hereby further amended to read as follows:

> No national banking association shall at any time be indebted, or in any way liable, to an amount exceeding the amount of its capital stock at such time actually paid in and remaining undiminished by losses or otherwise, except on account of demands of the nature following:
>
> First. Notes of circulation.
>
> Second. Moneys deposited with or collected by the association.
>
> Third. Bills of exchange or drafts drawn against money actually on deposit to the credit of the association, or due thereto.
>
> Fourth. Liabilities to the stockholders of the association for dividends and reserve profits.
>
> Fifth. Liabilities incurred under the provisions of the Federal Reserve Act.
>
> SIXTH. LIABILITIES AS INDORSER ON ACCEPTED BILLS OF EXCHANGE REDISCOUNTED AT HOME OR ABROAD, PROVIDED SUCH BILLS WERE NOT DRAWN OR ACCEPTED BY THE INDORSING BANK.
>
> The discount and rediscount and the purchase and sale by any Federal reserve bank of any bills receivable and of domestic and foreign bills of exchange, and of acceptances authorized by this Act, shall be subject to such restrictions, limitations, and regulations as may be imposed by the Federal Reserve Board.

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MEMORANDUM - RETIREMENT OF GREENBACKS.

The twelve Federal reserve banks shall be authorized and directed to assume all liabilities for the payment and redemption of all outstanding United States notes, commonly known as greenbacks, amounting to $346,681,016, and all outstanding United States Treasury notes of 1890, amounting to $2,254,000, and such banks shall be required to redeem any of such United States notes or Treasury notes which may be presented at their counters for that purpose, and shall also be required to reimburse the United States for any of such notes which may hereafter be presented to it for redemption and actually redeemed by it. Any United States note or Treasury note of 1890 hereafter redeemed either directly by the United States or by any Federal reserve bank on behalf of the United States shall be permanently retired and canceled and shall not be reissued. In exchange for the responsibilities and obligations imposed upon the twelve Federal reserve banks the Treasurer of the United States shall give and deliver to the various Federal reserve banks all of the gold now held in the Treasury of the United States as a gold reserve for the redemption of United States notes and Treasury notes of 1890, amounting to $152,977,036.63, and the Secretary of the Treasury shall be directed to issue to such Federal reserve banks, free of charge, one year gold notes of

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the United States and thirty year gold bonds of the United States in such proportions as he may deem advisable in an amount equal in the aggregate to the difference between the total amount of United States notes and Treasury notes now outstanding and the amount of gold hereinbefore directed to be given to such Federal reserve banks; such difference amounting to $195,957,979.37. Each Federal reserve bank receiving one year gold notes from the Secretary of the Treasury under the provisions of this Act shall enter into an obligation with the Secretary of the Treasury similar to that now required of Federal reserve banks which obtain one year gold notes in exchange for two per cent gold bonds of the United States under the provisions of Section 18 of the Federal Reserve Act. The total liability or obligation of any Federal reserve bank either to redeem directly or to reimburse the United States for the redemption of United States notes or Treasury notes of 1890, shall be limited to such proportion of the aggregate of such United States notes and Treasury notes as the capital and surplus of such Federal reserve bank shall bear to the aggregate capital and surplus of all Federal reserve banks provided, however, that the Federal Reserve Board may, from time to time in its discretion, make adjustments between the various Federal reserve banks so that the outstanding liability of such banks imposed by this Act will remain approximately in the same proportion. The one year gold notes, the thirty year gold

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bonds and the gold fund herein required to be given and delivered to the various Federal reserve banks shall be distributed to such banks in this same proportion under rules and regulations to be prescribed by the Federal Reserve Board. The notes and bonds of the United States herein provided for shall bear interest at the rate of three per cent per annum, but each Federal reserve bank shall pay to the United States each half year a tax at the rate of two per centum per annum on the average amount of such notes and bonds owned by it during such half year. Any Federal reserve bank which may acquire from time to time the notes or bonds of the United States provided for under the provisions of this Act shall have the right to deposit such notes or bonds with the Treasurer of the United States in the manner provided by existing law and shall be entitled 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 notes and bonds so deposited. Such circulating notes shall be obligations of the Federal reserve bank procuring them and shall be similar in form and shall be issued and redeemed under the same terms and conditions as Federal reserve bank notes authorized under the provisions of Section 18 of the Federal Reserve Act.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That the fifth paragraph of Section 13 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Acts approved March 15, 1915, and September 7, 1916, be and is hereby amended so as to read as follows:

Any member bank may accept drafts or bills of exchange drawn upon it having not more than six months8 sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. No Member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, or corporation to an ~~xx~~ amount equal at any time in the aggregate to more than ten per centum of its paid-up and unimpaired capital stock and surplus unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance and no bank shall accept such bills to an amount equal at any time in the aggregate to more than one-half of its paid-up and unimpaired capital stock and surplus; ~~xxxx~~ PROVIDED, HOWEVER, THAT THE FEDERAL RESERVE BOARD, UNDER SUCH GENERAL REGULATIONS AS IT MAY PRESCRIBE, WHICH SHALL APPLY TO ALL BANKS ALIKE REGARDLESS OF THE AMOUNT OF CAPITAL STOCK AND SURPLUS, MAY AUTHORIZE ANY MEMBER BANK TO ACCEPT SUCH BILLS TO AN AMOUNT NOT EXCEEDING AT ANY TIME IN THE AGGREGATE ONE HUNDRED PER CENTUM OF ITS PAID-UP AND UNIMPAIRED CAPITAL STOCK AND SURPLUS, PROVIDED, HOWEVER, THAT THE AGGREGATE OF ACCEPTANCES GROWING OUT OF DOMESTIC TRANSACTIONS SHALL IN NO EVENT EXCEED FIFTY PER CENTUM OF SUCH CAPITAL STOCK AND SURPLUS.

12-13-16

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 18 of the Act approved December 23, 1913, known as the Federal Reserve Act, be and is hereby amended by striking out from the second paragraph thereof the Proviso worded as follows:

> "Provided, 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 include bonds acquired under section four of this Act by the Federal reserve bank."

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 17 of the Act approved December 23, 1913, known as the Federal Reserve Act, be and is hereby amended so as to read as follows:

> Sec. 17. So much of the provisions of section fifty-one hundred and fifty-nine of the Revised Statutes of the United States, and section four of the Act of June twentieth, eighteen hundred and seventy-four, and section eight of the Act of July twelfth, eighteen hundred and eighty-two, and of any other provisions of existing statutes as require that before any national banking associations shall be authorized to commence banking business it shall transfer and deliver to the Treasurer of the United States a stated amount of United States registered bonds AND SO MUCH OF THOSE PROVISIONS OR OF ANY OTHER PROVISIONS OF EXISTING STATUTES AS REQUIRE ANY NATIONAL BANKING ASSOCIATIONS NOW OR HEREAFTER ORGANIZED TO MAINTAIN A MINIMUM DEPOSIT OF SUCH BONDS WITH THE TREASURER is hereby repealed.

12/12/16

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ASSOCIATE MEMBERS

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED,

That any bank or trust company incorporated by special law of any State or organized under the general laws of any State or of the United States shall be entitled, under such rules and regulations as the Federal Reserve Board may prescribe, to become an associate member bank of the Federal reserve bank of the district in which it is located. Any State bank or trust company which has become an associate member under the provisions of this Act and the regulations of the Federal Reserve Board shall have the privilege of clearing and collecting checks through its Federal reserve bank and shall have all the rights and shall be subject to all the restrictions imposed by law, by the regulations of the Board, or by the regulations of the Federal reserve banks upon their respective member banks in so far as they relate to the clearance of checks through Federal reserve banks. Clearing members are hereby required to maintain the same balances with their respective Federal reserve banks as are now required to be maintained by member banks under the provis provisions of the Federal Reserve Act. The rules and regulations of the Federal Reserve Board governing the admission of associate members shall provide, in addition to such other requirements as the Board may specify, that each associate member shall satisfy the Federal reserve bank of its district at the time of its admission, or at any other time, as to the financial condition and each Federal reserve bank is hereby authorized to provide for special examination of any associate member at such time or times as may be deemed advisable in order to procure information necessary to determine their condition.

The Federal Reserve Board may upon thirty days' notice suspend from membership any clearing member which has failed to comply with the provisions of law or the regulations made in conformity therewith.

Any provisions of law inconsistent with this Act are to that extent and to that extent only hereby repealed.

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THE FEDERAL RESERVE SYSTEM

AS A NEW FACTOR

IN NATIONAL AND INTERNATIONAL FINANCE

Address by W. P. G. Harding,

Governor, Federal Reserve Board.

To the Boston City Club,

Boston, Mass., on Thursday
evening, December 14, 1916.

For release to
morning papers of
Friday, December 15th.

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Daniel Webster, in his Reply to Hayne, began with these words:

"When the mariner has been tossed for many days, in thick weather, and on an unknown sea, he naturally avails himself of the first pause in the storm, the earliest glance of the sun, to take his latitude, and ascertain how far the elements have driven him from his true course. Let us imitate this prudence, and before we float further on the waves of this debate, refer to the point from which we departed, that we may at least be able to conjecture where we now are. I ask for the reading of the resolution." Sixty years later the same idea was epitomized, not elegantly, but tersely, by an Alabama Congressman, who, having been interrupted in the course of debate, resumed his remarks with the question, "Mr. Speaker, where was I at?"

It seems proper, in these momentous times, with half the world in the throes of a death struggle, when the breaking of precedents, the establishment of new records in all lines of business, and the appearance of new problems - industrial and financial - are matters of daily occurrence, that American business men and bankers whose function it is to think and to act for others as well as for themselves, should make careful and constant reckonings, in order to determine where we now are,

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and how far the storm on the other hemisphere is driving us out of our normal course.

Few, if any, will contend that general business conditions in the United States today are normal. Our export trade for example, has increased from one and one-quarter to one and one-half billions per annum in ordinary times, to between five and six billions. We have received since January first 1915 importations of gold into this country in settlement of trade balances amounting to more than one billion dollars, and within that time we have sent to other countries about a quarter of a billion in gold, so that the net increase in our gold stock in about two years' time has been around seven hundred and fifty millions of dollars. We have witnessed a marked rise in prices of all commodities, - meats, farm products, metals, and manufactured goods, and have seen repeated advances in wage scales, so that costs of production have been greatly increased and the cost of living has reached a point hitherto unknown in times of domestic peace. Just as surely as night follows day, so is action succeeded by reaction, and thoughtful men are turning their eyes to the future and are seeking means for building up a permanent trade in those articles of commerce for which there is normally a steady demand, and with those countries which may reasonably be depended upon to become permanent customers.

Frankly, we know that much of our present prosperity has come to us as a result of calamities to others, and that

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radical changes must necessarily occur when swords are beaten into plow-shares and peace resumes its sway. No man whose heart-beats respond to the instincts of humanity would wish to see a prolongation of war for the sake of personal gain or national aggrandizement, but it is only natural that we should wish that the changes which must occur with the return of peace be followed by gradual and moderate reactions rather than by a perpendicular slump in business and by general financial disturbance. I must confine my remarks tonight to a brief discussion of the relation of the banks of this country to the present situation and to the changing conditions which are to come. While there are serious responsibilities which must be borne by all the banks, I feel that our new banking system, composed of the twelve Federal Reserve Banks, is charged particularly with the obligation of leadership and of providing means of assisting our financial institutions to meet successfully any situation which may arise. History shows that after every great war there is an aftermath, - a period of reconstruction which requires not only financial leadership of the highest order, but intelligent cooperation and concentration of capital. For several years after the close of the Revolutionary War financial conditions in this country were chaotic; Continental currency was without value, such currency as we had was local and even personal in its character, and we were entirely dependent upon

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foreign countries for the limited amount of coin that was in circulation or that was held in strong boxes. Closely following the establishment of the Federal government, and mainly through the instrumentality of Alexander Hamilton, the first bank of the United States, a central bank modeled somewhat along the lines of government banks in Europe, was chartered in the year 1791, for a period of twenty years. Through its aid the finances of our young republic were placed upon a firm foundation and a stable and uniform currency system was established. But even in those early days there was a strong prejudice against a central bank as being contrary to the genius of our American institutions; and when the charter of the bank expired in 1811 it was not renewed by Congress.

Then followed the War of 1812 and upon it conclusion it was found that the resources of the independent banks which had come into existence could not be coordinated in such a way as to meet the situation successfully, and so in 1816 Congress chartered the second Bank of the United States, another central bank. The antagonism however, to the central bank idea had never died out, and the latent sparks of opposition finally burst into flame, so that in 1836 the Bank of the United States ceased to exist as a national bank and was forced a few years later to wind up its affairs. From the days of Andrew Jackson there has never been a time when a majority of the people of the United States have been in favor of one central banking institution. While certain

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advantages growing out of such a bank have been recognized, they have been more than offset in the public mind by the inherent evils and possible dangers of such a system. In the midst of the Civil Was in 1863, the National Banking Act was passed by the Congress of the United States, and provided a system of banking in this country that was dominant for fifty years and which is the corner stone of our present Federal Reserve system. The first and perhaps paramount purpose of the National Banking Act was to provide a uniform national system of currency, without the creation of a great central institution like the old bank of the United States. The national banks were subjected to uniform laws, and to government supervision, but they were disjointed units, and no means were provided by law for any concentration of their resources in times of need. Any effective cooperation between them was voluntary, through clearing house associations, and the measures adopted by them to meet various crises, while necessary and commendable, were of questionable legality.

The status of the national banks prior to the advent of the Federal Reserve system may be likened to that of the thirteen original states of the American Union during the years that intervened between the recognition of their independence and the adoption of the Constitution. The Federal Reserve Act of December 23, 1913, which has provided a bond of union between the banks is entitled "An Act to provide for the establishment of Federal Reserve Banks, to furnish an elastic currency, to afford

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means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes." Section 18 of the Federal Reserve Act provides means, at the option of national banks, for retiring the whole or any part of their circulating notes by authorizing the Federal Reserve Board to require the Federal Reserve Banks to purchase bonds from the national banks in an amount not exceeding $25,000,000 in any one year, which bonds may be exchanged, under the conditions stated in the Act, for United States 3% 30-year bonds and 3% one--year gold notes, without the circulation privilege. The intention of the framers of the Federal Reserve Act was undoubtedly to provide, through the gradual retirement of national bank notes, a vacuum to be filled by issues of Federal Reserve notes, But I am getting ahead too rapidly and this phase of our currency question will be considered later on in my remarks.

When the bill to establish national banks was introduced in Congress in 1863, less than thirty years had elapsed since the withdrawal of the Treasury deposits from the bank of the United States. The opposition at that time to a central bank, or to any institution carrying with it a centralized control, was deepseated and widespread, and the sponsors of the various plans which took final shape in the National Banking Act were careful to point out that the objections to a central bank had been duly considered and had been avoided by them. It was first suggested that State banks and bankers be permitted to issue circulating notes secured by United States bonds, and it was urged that

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none of the objections against a central bank could be offered against such a plan, and as the Government would have no power to bestow favors, such a system could not be used for political ends. In a speech advocating this plan Samuel Hooper, a member of the House from Massachusetts, said: "As far as the United States Bank is concerned, it was affirmed that, by its favors, the Government enabled that bank to monopolize the business of the country; and it was affirmed that frequently great inconvenience and sometimes terrible disaster resulted to the trade and commerce of different localities by the mother bank of the United States arbitrarily interfering with the management of the branches by reducing suddenly their loans and sometimes withdrawing large amounts of their specie, for political effect. Here each bank transacts its own business upon its own capital, and is subject to no demands except those of its own customers and its own business. It will be as if the Bank of the United States had been divided into many parts, and each part endowed with the life, motion, and similitude of the whole, revolving in its own orbit, managed by its own board of directors, attending to the business interests of its own locality; and yet to the bills of each will be given as wide a circulation and as fixed a value as were given to those of the Bank of the United States in its palmiest days."

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In the second annual report of Honorable Hugh McCulloch, the first Comptroller of the Currency, made in November 1864, the new banking system is discussed at length, and regarding it the Comptroller said: "It promises to give to the people that long-existing 'desideratum', a national currency, without a national bank, a bank note circulation of uniform value without the creation of a moneyed power in a few hands over the politics and business of the country."

The banks established under the National Banking Act are, and were designed to be local institutions, independent of each other, but under national control and supervision. Nationalization without centralization is the keynote of the National Banking Act, under which, as originally enacted, each national bank was required to designate specifically the State, county and city, town or village, as the place where its operations of discount and deposit were to be carried on, and was allowed only one place of business, no branches or branch offices being permitted; and, while by the amendment of May 1, 1886, a national bank is authorized to change its location, it must be to a place not more than thirty miles distant and the new location must be in the same State as the old. The local character that was intended to be given a national bank is further emphasized by the requirement that the rate of interest which a bank may charge must not exceed the rate allowed by the laws of the State, territory or district in which it is located; nor are national banks permit-

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ted to acquire stock in other banks or to retain such stock when taken to secure a debt previously contracted, except for a reasonable time pending its sale; but under the Federal Reserve Act a national bank is expressly required to be a continuing stockholder in the Federal Reserve Bank of its district.

Notwithstanding the purpose to localize each national bank as far as its situs is concerned, no geographical limitation is placed by the law upon the deposits that may be received by a bank or upon the loans which it may make, although the bank is expressly prohibited from transacting its business in more than one office and is without power to establish a branch even in its own town; but on the contrary every national bank has the right to solicit and to receive deposits from, and to make loans to, individuals and corporations in all parts of the United States and of the world. Further than this, the National Banking Act originally provided that national banks in eighteen cities might be used by national banks in all other cities as custodians of a part of their required reserves and the banks in seventeen of these reserve cities were authorized by the Act to carry one-half of their required reserves with banks in New York City, an inconsistency typical of the composite character of much of our legislation; for while the National Banking Act made possible any number of individual banking units it not only permitted but compelled the concentration of a considerable part of the banking reserves of the country

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with the banks of a single city. The Federal Reserve Act is more consistent. While it recognizes the advantages of a concentration of reserves, it does not create a central or dominant institution, but provides instead for the establishment of twelve banks, each to act as a central bank for the reserves of its own district, the stock of each to be owned by, and its deposits to come from, banks in its own district and from none other. In this manner the reserves of the different sections of the country are designed to be kept at home, and undue concentration in a single city or in a small group of cities is avoided. A large national bank in Boston or in New York can so extend its business as to solicit and receive deposits and to make loans without any restriction as to locality, counting among its customers corporations, firms, and individuals in all parts of the United States and in foreign countries; but the Federal Reserve Bank of Boston or the Federal Reserve Bank of New York can deal only with banks in its own Federal Reserve district. Any Federal Reserve Bank can engage in open market operations resulting from transactions which may have originated in other districts, and may rediscount for other Federal Reserve Banks, but no Federal Reserve Bank has the same wide field of operation throughout the country as a whole that is open to the national banks. While the Federal Reserve Banks are legally autonomous units there is no power given to them to act with other Federal Reserve Banks by virtue of agreements made by their

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directors or executive offieers so as to constitute themselves a system with centralized powers, but the control of the Federal Reserve Banks in this respect is vested in the Federal Reserve Board, through which body alone the coordinated and centralized powers of the Federal Reserve system are exercised; and even in the creation of the Federal Reserve Board the danger of localized contralization is recognized and guarded against, for the Federal Reserve Act provides that in the designation of the five appointive members of the Board the President shall select not more than one from any one Federal Reserve district and that he shall have "due regard to a fair representation of the different commercial, industrial and geographical divisions of the country." While the main purpose of the National Banking Act was to provide a national currency without the intervention of a central bank, its development and operation made possible a greater concentration of banking power in the hands of a few individuals than the country had ever known before; but the Federal Reserve Act has provided for the concentration of reserves in a carefully controlled central institution in each of twelve geographical divisions of the United States, and when necessary, for the mobilization of the resources of these institutions as one great bank, thus avoiding the dangers that would come from a single centralized institution while affording all the safeguards and benefits to be derived from concentration and cooperation.

Some of you may perhaps have seen a statement that was recently given to the press by the Federal Reserve Board, in which

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the suggestion was made that in view of abnormal conditions throughout the world, it would be best that the banks of this country should keep themselves in a liquid condition and proceed along indicated lines of prudence and conservatism. The suggestion was made also that as the United States is fast becoming the banker of foreign countries in all parts of the world, investors should receive full and authoritative data, particularly in the case of unsecured loans. I know that there has been criticism of the Board's action in making this statement, which has been given a significance neither justified nor intended. In its reference to investors, it was not the purpose of the Board to make an attack, either open or covert, upon the credit of any government, nor did it seek in its statement to reflect upon any particular obligations. In my opinion, what the Board had in mind when it made its brief reference to investors, was simply this. American investors have for many years been accustomed to buying industrial securities - railroad obligations to a great extent. In dealing with these securities certain well established rules have been developed. The investor has acquired the habit of requiring specific information regarding gross earnings, fixed charges, net earnings, sinking funds, etc., and he insists upon knowing definitely whether he is offered a first mortgage bond, income bond, preferred stock, or common stock. It is the practice of every issuing house when offering securities to state all necessary details either over its own signature or that of the head of the borrowing cor-

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poration. Nowhere is the importance of authentic and complete information more fully understood and appreciated than in Europe, both in England and on the Continent, and prospectuses for foreign loans contain all the important facts relating thereto, in a statement signed by an authorized representative of the foreign government or by the issuing house, or in some cases by both. The Board sought merely to call attention to the fact that as this country has become an important market for foreign securities, the same businesslike habits which are well established regarding domestic loans, should be developed in the marketing of foreign flotations.

It happened that a few days after the Board's statement had been made public, certain momentous events took place which had no connection whatever with any domestic incidents. Last week there was a notable stiffening in rates for call loans in the New York market , which advanced to 15%, a higher level than they had reached since the establishment of the Federal Reserve Banks. One of the leading financial journals, in an editorial discussing this incident, has this to say:

> "The pinch in money at this centre thepresent week, under which rates for call money on Monday touched 15% and reached maximum figures of 10% on Tuesday and 7% on Wednesday (normal conditions not being restored until Thursday), demonstrates anew that the Federal Reserve system, upon which the whole country has been placing so much dependence, has not solved our monetary problems. If, prior to the experience of this week, any one had ventured to suggest that such high rates were possible with the Federal Reserve system in full operation and at a time when the country is literally flooded with currency in one form or another, he would have been deemed lacking in perfect :

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faith and denominated a hopeless skeptic. These high rates, too, have come at a time when the gold stream to these shores from foreign countries has been flowing with such strength and volume that many good people have been holding up their hands and saying that we are getting too much of the metal and that the movement ought to be stopped. As it happens, the easing of the monetary tension here which came towards the end of the week was due entirely to the resumption of gold imports on a large scale, and it is evident that whatever may be the situation elsewhere in the United States, New York has been badly in need of extra supplies of gold."

It may seem paradoxical and certainly is anomalous that while the country is literally swimming in gold as the result of the enormous importations of the metal which have occurred since the beginning of 1916, the New York Clearing House banks and trust companies should be steadily drained of their supplies of the metal, and of their money holdings generally, yet the fact itself can not be gainsaid. And it is a striking commentary upon the working of the Federal Reserve system that this should be so. Secretary of the Treasury McAdoo in his annual report the present month is loud in his praises of the Federal Reserve system and of the benefits it has conferred upon the community, but in view of this week's happenings his flattering tribute would appear somewhat premature.

The Secretary avers that the country's present "great prosperity could not exist without it (the Federal Reserve system)." This is perhaps pardonable exaggeration, but has no basis in the facts. Nor is there warrant for the contention that "the usefulness of the system has been broadened recently by the amendatory Act of September 7, 1916." On the contrary, through these amendments and the methods pursued in the administration of the law, nearly all of which have tended to promote the inflation possibilities of the law, there has been a distinct departure from the conservatism that marked the statute as originally drafted and the law has lost some of its most potent elements for good.

Certainly the Reserve Act must be held responsible for the depleted state of the Clearing House institutions at this centre. For it is the reduction in the money holdings and surplus reserves of these Clearing House institutions that accounts for the twist in money; and the possibility of such a flurry in money rates as has now occurred would have been sooner

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recognized except for the implicit faith felt in the efficacy of the Reserve system, which has made the ordinary man inclined to neglect his customary study of monetary currents. It has been argued that business activity, together with high prices and Stock Exchange speculations, necessarily create an active demand for loan accommodation. That of course is in considerable measure true, but the predicament in which the Clearing House banks found themselves this week was not due to loan expansion but followed directly from a severe loss in money holdings. The existence of the Federal Reserve Bank at this centre has not served to relieve the situation and there is no telling what might have happened except for the opportune arrival of some more gold from abroad.

* * * * * * * * *

It is noteworthy that the large credit balances of the Federal Reserve Bank of NewYork did not serve to swell the Reserve Bank's own money holdings, showing that the money must have been transferred to other points by the Reserve Bank through the Reserve clearing house system. As a matter of fact, the New York Reserve Bank's money holdings, after being heavily enlarged in the week ending November 17, (when the total of gold and legal tender mounted from $170,660,757 to $192,852,297), were in the succeeding two weeks reduced to $156,408,741, at which figure the total was the smallest of any week since June 2 last. In other words, the Federal Reserve Bank of New York drew enormous amounts out of the Clearing House institutions and could not retain the money, but transferred it, as already stated, to other points. "

It seems that this high authority is an unwilling witness to the soundness of the position taken by the Board in its statement, although it takes occasion to rap the Federal Reserve system. But it is difficult to see how the New York Federal Reserve Bank can be held responsible for the depletion of reserves of its member institutions, or in what respect its operation has been unfair to the banks of its home city. Besides being our chief financial center, New York is our greatest port of entry. Through its custom house

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passes a vast volume of goods which do not remain in New York City but which are distributed throughout every State to every town and hamlet in the land. In the same way most of our imports of gold come first to New York, and through the financial institutions there find their way to other sections of this country and to South American nations. The Federal Reserve Bank does not cause this diversion of gold; it merely aids its member banks in effecting the distribution called for by our commercial transactions. It is rather amusing to find in the same issue of the financial journal to which I have referred, - which in its editorial states that the existence of the Federal Reserve Bank in New York has not served to relieve the situation, and there is no telling what might have happened except for the opportune arrival of some more gold from abroad, - this statement in its reading columns:

NEW YORK CITY BANKS AVAIL OF REDISCOUNT PRIVILEGES OF RESERVE BANK.

"The use of the rediscount privileges of the Federal Reserve Bank was availed of for the first time this week by several of the local banks. While the practice is new to the banks of this city, the up-State banks are said to have made use of the rediscount facilities of the Reserve System ever since the opening of the Reserve Bank. So far as the New York institutions are concerned, the New York Federal Reserve Bank is said to have taken the initiative in suggesting that they adopt the practice of rediscounting through it. It is explained that their action in resorting to the Reserve discounting privileges was not the re-

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sult of any apparent strain of the money market, but to inaugurate this feature of the system and demonstrate its workability."

It is a noteworthy fact that except for a slight advance in the hitherto abnormally low rate for acceptances, there has been no advance in rates for commercial paper of a character eligible for rediscount with Federal Reserve Banks, and the so-called "flurry" was confined entirely to loans secured by stock exchange collateral. While the Federal Reserve Act does not permit Federal Reserve Banks to rediscount paper secured by investment securities such as stocks and bonds, national banks which carry such loans can at any time strengthen their position by rediscounting eligible commercial paper with the Federal Reserve Bank, and it seems that the important banks in New York and Boston which had rediscount transactions a few days ago with their Reserve banks, desired to impress this fact upon banking institutions throughout the country. Hitherto large banks have as a rule not been inclined to show any rediscount liability upon their statements, and an aversion to rediscounts has been felt by many of the smaller institutions throughout the country. The Federal Reserve Act, however, while imposing strict limitations upon the character of the paper that can be discounted by Federal Reserve Banks, distinctly encourages rediscount operations by member banks, and before the amendment of September 7, 1916, permit-

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ting Federal Reserve notes to be issued upon the security of bills purchased in the open market, it was impossible to issue Federal Reserve notes except upon paper rediscounted by a member bank. It is highly important, in the proper development of the Federal Reserve system, that banks should overcome their old-time prejudice against rediscounting and that they should learn to avail themselves freely of the facilities afforded by the Federal Reserve Banks.

In the statement to which I have already referred, the Federal Reserve Board announced that it does not share the view frequently expressed of late, that further importations of large amounts of gold must of necessity prove a source of danger or disturbance to this country. That danger, in the opinion of the Board, will arise only in case the inflowing gold should remain uncontrolled and be permitted to become the basis of undesirable loan expansions and of inflation. The Board suggested that there are means of controlling accessions of gold by proper and voluntary cooperation of the banks, or, if need be, by legislative enactment. It suggested that an important step in this direction would be the anticipation of the final transfer of reserves required by the Federal Reserve Act to be made on November 16, 1917. A bill has been introduced in Congress providing that this transfer be made effective with-

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in sixty days from the date of its enactment. There are now approximately $600,000,000 of so-called reserves held by national bank reserve agents which, if the amendment becomes a law, and in any event, in November 1917, will no longer be counted as such, but will have the status simply of balances in bank. The actual reserve requirements in gold will be increased by about $200,000,000, and if we do not regard profit as a first consideration, there are other means by which the continued inflow of gold into this country can be used to its lasting benefit.

For many years this country has been handicapped because of the inelastic quality of a very large part of its circulating medium. I refer particularly to the legal tender notes or greenbacks, and to national bank notes. The framers of the Federal Reserve Act had in mind the ultimate retirement, over a period of twenty years, of the bond-secured national bank notes, and the conversion of the United States 2% bonds upon which they are based; but in the permissive form in which this section of the Act was finally passed, there is no certainty that the national bank notes will be retired, nor will I go so far as to say that the retirement of all national bank notes is desirable or necessary in our present situation. I have heard the suggestion made that it might be well to consider the adviasbility of preparing for the retirement of say, $200,000,000 of national bank notes within the next three years,

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provided this can be done without injury to the national banks and without permanently contracting our circulating medium, in case it should ever be desirable to keep it at its present volume. An Act of Congress would of course be necessary to carry into effect any plan for the compulsory retirement of national bank notes, and I have made this reference merely to show that our circulating medium need not necessarily become redundant by further injections of gold into it. Treasury notes possessing legal tender qualifications, are outstanding to the extent of $348,721,925, of which $346,681,016 are the old war time greenbacks and $2,040,909 are Treasury notes of 1890 which were issued on account of silver purchases but which are payable in coin. The suggestion has been made frequently that advantage should be taken of the present plethora of gold to retire permanently these notes. No doubt some of the opposition which manifested itself in the late sixties and the early seventies against the retirement of legal tender notes may spring up again, should their retirement be seriously considered. But if our currency is redundant, would it not be wise to strengthen it by retaining gold, at the same time retiring the notes that have caused so much controversy and disturbance in times past? The principal objection will probable come from those who may fear that the retirement of the legal tender notes will lead to permanent contraction, but if they could be convinced that this is not the case and that the

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vacuum created could be filled at any time when necessary by Federal Reserve notes of a truly elastic character, their opposition would have little to rest upon. If Congress should ever decide upon the retirement of the greenbacks, the Federal Reserve Banks could be utilized as a means of effecting the operation, without the slightest disturbance to interest rates or to credit facilities.

So far any influence the Federal Reserve Banks have exerted in the field of international finance apart from their importance as the holders of domestic reserves, and their position when considered collectively, as a dominant factor in American banking, has come from their ability to purchase or discount acceptances arising out of transactions involving the importation or exportation of goods. Later on, in all probability, the Federal Reserve Banks will avail themselves of the powers given them by law, with the consent of the Federal Reserve Board, to open and maintain banking accounts with foreign countries and to establish correspondents and agencies abroad, but so far they have done nothing in the foreign field except to encourage the development of the acceptance business, which is already playing a very important part in financing our commercial transactions abroad. The Federal Reserve Act authorizes national banks to establish branches in foreign countries, and the amendment of last September permits them to become stockholders in corporations organized for the purpose of carrying on a banking business in other countries. Already two American banks have established branches in the West Indies and in South

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America, and it is thought that their example will be followed by other banks in the course of time.

Two years have elapsed since the establishment of the Federal Reserve Banks. While they have not been operated with an eye to profit, they have earned their expenses and a part at least of their dividend requirements. The prejudices which existed in the beginning against the Federal Reserve system have to a great extent disappeared. The Reserve banks had not been established in the summer of 1914 when the country was brought face to face with a great crisis because of the outbreak of the European war, and since their organization they have had no opportunity to give a practical demonstration of their efficiency as emergency institutions, and because of the remarkable ease in money which has existed almost continuously during the past two years, they have not had the opportunity of exercising to any great extent all of the functions for which they were designed. They have nevertheless gained steadily in the confidence of the public, and the fact of their existence has enabled the country to withstand, without the slightest financial disturbance, many shocks and sensations which would probably under old conditions have been followed by unpleasant results. I think it may be said in all fairness that the Federal Reserve system is no longer looked upon as an ephemeral experiment. The country recognizes that

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it has been established upon a firm and enduring foundation, that it has not been and can not be conducted for the sole benefit of any group or interests, but that the policies governing its operation are, and must continue to be, broad enough to serve the banks and the patrons of banks, without discrimination throughout the entire country. The Federal Reserve law as it stands may not be perfect, but we have every reason to believe that the country feels that it is correct in principle and that any changes which may be made in the law from time to time will be along lines which enable the Federal Reserve Board and the Federal Reserve Banks better and more adequately to provide for all contingencies, and to measure up more fully to the duties and responsibilities which have devolved upon them.

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FEDERAL RESERVE BOARD

WASHINGTON

M.C.Elliott
Counsel.

November 22, 1916.

My dear Mr. Delano:

I have read the attached letter from Mr. Brown, Chief of the Bureau of Efficiency, dated October 16, 1916, in which he takes exception to memorandum of this office dated July 18, 1916.

It appears that my memorandum is construed as a criticism of the Bureau of Efficiency. It was not so intended. I was not aware that the present centralized system of collections and disbursements in use in the Treasurer's office was installed at the instance of this Bureau.

It was my purpose merely to call to the Board's attention the fact that Congress clearly intended that Federal reserve banks should be used as fiscal agents of the Government and that they could be used in the collection and disbursement of Government revenues to the advantage of the Government and of the banks.

In view of Mr. Brown's criticism it has seemed advisable to reply to his letter in some detail. I am accordingly handing you supplementary memorandum explaining the position of this office.

Very sincerely,

M. C. ELLIOTT

Hon. F. A. Delano,
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

M. C. Elliott
Counsel.

November 21, 1916.

Memorandum for the Board:

In a letter dated October 16, 1916, Mr. Herbert D. Brown, Chief of the Bureau of Efficiency, takes exception to memorandum filed with the Board by this office under date of July 18, 1916.

In this memorandum the suggestion was made that the several Federal reserve banks could be used to advantage by the Government in the collection and disbursement of revenues. Briefly summarized, Mr. Brown's criticisms of this memorandum appear to be as follows:

1. That the memorandum contained several inaccuracies. These so-called inaccuracies apparently consist of the following suggestions:

(a) That checks drawn against the Treasurer of the United States are not properly scrutinized before payment.

(b) That stoppage of payment on checks and tracing of items after payment is difficult.

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2. That it was not demonstrated in what way any saving in expense might result from the adoption of the plan proposed in the memorandum of July 18.

3. That the present system has all of the advantages without the disadvantages of the plan proposed in the memorandum of July 18.

4. That the adoption of the plan proposed in the memorandum of July 18 and the transfer of accounts from the Treasury to the Federal reserve banks would prevent important economies in handling the checks that can be effected if the accounts remain in Washington.

Answering these criticisms in the order in which they appear -

1. It appears from Mr. Brown's letter that the only examination of checks made by the Treasurer's office (before payment) to determine whether such checks have been properly issued and negotiated consists of a visual comparison of the signature on the check with the autograph signature of the disbursing officer kept on file for that purpose; that no examination is made to see whether the checks are dated or whether they show from what place they were drawn; that they are not examined to see whether the payee has indorsed;

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whether the subsequent indorsements are regular; or whether the last indorsement is that of the bank whose transcript the check accompanies; that no examination is made to determine whether the amount shown in figures corresponds with the amount written in the body of the check; nor is any examination made to see whether the check has been altered in any way either in the figures or in the amount written in the body of the check.

Mr. Brown contends that the Auditor and not the Treasurer should examine the indorsements if this is deemed necessary; that the checks are not examined to see whether the payee has indorsed, as this would involve an extra expense to the Government of $5,000 a year; that if any irregularity in indorsement is later discovered the indorsing banks are liable and the Government runs no risk of loss.

In reply to these criticisms it is respectfully submitted -

The Government owes a Duty to the Banks to Adopt all Proper Safeguards.

Inasmuch as the Government requires depository banks and Federal reserve banks to cash its checks or warrants at par, it owes a duty to all such banks to provide

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every safeguard against the payment of items irregularly drawn or negotiated. The mere fact that the Government is protected and may have recourse against a prior indorser is not a justification of failure on its part to properly scrutinize checks before payment. If a forgery or irregular indorsement is promptly reported to the prior indorsers, they may take steps to protect themselves, but delay in the discovery of an irregularity makes it difficult for them to procure relief. As an evidence of this fact I am advised that there is now pending in New York a friendly suit to test the question of whether or not the Government may recover from a prior indorser on a forged check which the Treasurer's office paid, and on which the forgery was not discovered for three or four months after payment.

It appears that in this case a check was drawn for three or four thousand dollars, the signature of the drawer and first indorser both being forged. It was received from the Chase National Bank about the middle of September, 1914, and the bank allowed credit therefor the next day. The disbursing officer was simultaneously charged with the amount, which overdrew his account. This resulted in an investigation which, early in January, 1915, disclosed the forgery, at which time the Chase National Bank was directed to credit the Treas-

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urer with the amount of the check. The bank declined and the friendly suit resulted. Except for the overdraft created it is possible that the forgery would not have been discovered as soon as it was.

I am advised that checks are frequently returned by the Auditor for the Treasury Department to the Treasurer of the United States on account of irregular indorsements; that in many instances the checks are not indorsed by the payee at all and in some cases bear no indorsement whatever.

The mere examination of the signature of the disbursing officer can hardly be said to afford proper protection to prior indorsers. To the extent that it is effective it will protect against forgeries but not against irregular negotiation. It appears that the Treasurer's office, under the present system, handles an average of ten million checks a year or an average of over thirty-three thousand a day if the force works full three hundred working days in a year. To detect irregularities in signatures by a visual comparison with guide cards necessarily involves the employment of clerks which are more or less expert in the matter of handwriting.

An individual bookkeeper in a bank having to sort and enter checks in detail naturally becomes more familiar with

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the signature of a depositor than is possible when a large volume of checks are merely compared with autograph signatures on cards, and if this system is to prove effective those making comparisons must be to all intents and purposes handwriting experts.

The Drawee's Scrutiny should be more Thorough Than that of a Bank Handling the Item in Transit.

As long as a check is in transit the indorsing bank relies and may reasonably be expected to rely to a great extent on the prior indorsements. When, however, a check reaches the drawee and is to be charged up to a depositor's account the drawee should see that the check constitutes a full legal authority for its payment, and must necessarily scrutinize it with greater care than banks through which it has been sent for collection. It necessarily follows that any examination for irregularities should be made before rather than after payment.

It is true that the Auditor must pass upon the legality of the disbursement evidenced by the check, and the remitting bank, even though given credit by the Treasurer, may, nevertheless, have the item returned if the Auditor disapproves payment. It is, therefore, important that the records of the Treasurer's office should be kept so as to facilitate the tracing of items

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after payment, and the prompt return to the remitting bank of checks drawn ro cover unauthorized or illegal disbursements.

It is submitted, however, that before checks leave the office of the Treasurer they should be carefully examined to determine whether they have in form been properly drawn and negotiated, thus limiting the checks returned by the Auditor to those which represent unauthorized disbursements.

Tracing Items after Payment by the Treasurer.

On this subject Mr. Brown says:

> "It is true that for the sake of economy receipts and payments are entered on the books of the Treasurer's office in totals and that the totals are obtained from adding machine lists of the amounts only, without descriptive entries, so that an item can be traced into the ledgers through the adding machine lists only by its amount."

I understand that under the present system checks received from remitting banks are accompanied by a transcript prepared by the bank on which the checks are listed by symbol number, serial number, and amount.

When the mail is opened the banks' transcripts with accompanying checks are placed in boxes or files designed for this purpose, and the contents of each box is treated as a group and is designated by a letter of the alphabet select-

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edfor that purpose. These groups are then turned over to what is called the proving section of the Treasurer's office. In order that each check and transcript may thereafter be identified as belonging to that group, the checks and transcripts are then perforated with a machine which cancels the check and shows the date of payment and group letter. The checks are then proved against the transcripts which they accompany, after whichthey are sorted according to the symbol of the disbursing officers. When this has been done the signatures are compared and the checks drawn by each disbursing officer are then run off on an adding machine and the total of all checks of each disbursing officer is charged to his account in the ledger. The total of all disbursing officers' checks must, of course, agree with the total of all transcripts sent in by the bank. The checks are then sent to the Auditor. If the Auditor later discovers an irregularity in a negotiation of the check or if it appears that the check has been drawn for an unauthorized purpose, it is returned to the Treasurer. If the last indorsement is regular the Treasurer can immediately determine what bank sent it in by this indorsement. If the remitting bank has failed to indorse, the Treasurer's office must determine by the perforation in what group the remitting bank's transcript

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is filed, and must then identify the check by symbol number and amount shown in the transcript of the remitting bank.

As there are more than seven hundred banks making such remittances, this trace involves some labor and this labor is increased if the irregularity is not discovered until some days after payment. If the Federal reserve banks handled these checks each item could be entered in the individual ledger account of the disbursing officer - the Treasurer would receive only twelve instead of seven hundred or more transcripts with checks already assorted according to disbursing officers and the work would unquestionably be simplified.

SECOND. Expenses under Present System.

The memorandum of July 18 was intended merely as an outline of a plan and no attempt was made to consider the details of operation.

It is manifest, however, that if the sorting and handling of a large proportion of the checks now handled by the Treasurer's office can be transferred to the Federal reserve banks the work required of the Treasurer's office will be materially reduced. The added expense to the Federal reserve banks would be offset by an increase in their deposits. These de-

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posits would contribute to the earnings of the Federal reserve banks and would no doubt more than defray the expenses of handling the checks in question. The Government would, therefore, save part of the expense now incurred by the Treasurer's office, and would benefit by the increased earnings of the Federal reserve banks, since all the profits of such banks over and above dividends and expenses are paid to the Government after a reasonable surplus has been created.

In the matter of reduction of expenses in the Treasurer's office, Mr. Brown estimates that it would cost $5,000 a year merely to examine the checks to see that the payee has indorsed. It necessarily follows that it costs several times this amount (a) to prove the transcripts, (b) to sort the checks, (c) to make a visual comparison of the signatures, (d) to run them off a second time on adding machines, and (e) to perforate each check so as to connect it with the bank's transcript.

This expense would in large part be saved.

To determine with any accuracy the amount that could be saved would involve an investigation of the details of the work of the Treasurer's office, but it seems evident that if the Federal reserve banks can absorb a large part of this work without added expense and with a possible profit, a saving could be

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effected of a considerable amount.

THIRD. Centralization v Decentralization.

Mr. Brown argues at some length that the present system has practically all of the advantages without the disadvantages of a decentralized system.

In support of this argument he points out -

(a) That the majority of the officers who have occasion to consult the accounts or to be consulted with reference to them are located in Washington.

(b) That the administrative officers having supervision over the disbursing officers are located in Washington.

(c) That approximately sixty per cent of all checks are issued at Washington.

(d) That the bulk of credits originate here.

(e) That daily and monthly statements of the condition of the Treasury are prepared here and are taken from controlling accounts kept in Washington.

He suggests that if the accounts were carried elsewhere there would be delay -

(f) In the entry credits to disbursing officers.

(g) In furnishing information regarding balances.

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(h) In reporting irregularities.

(i) In filing the majority of notices to stop payment on checks.

(j) The collection of information for the daily and monthly statements.

Considering these suggestions in the order in which they appear:

(a) The accounts of the Treasurer would, of course, continue to be maintained in Washington under the plan proposed in memorandum of July 18. The twelve Federal reserve banks would be substituted as depositories for the 700 or more depository banks referred to by Mr. Brown. They would relieve the Treasurer's office of the detail work of handling checks of many of the disbursing officers and it is believed that the work of the Treasurer's office could be very much simplified.

(b) The heads of departments and bureaus necessarily have supervision over a great many subordinates including disbursing officers located elsewhere than in Washington. The presence in Washington of subordinate officials is not essential to effective supervision.

(c) Mr. Brown estimates that sixty per cent of the Government checks originate at Washington; that fifty per cent

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of all Government checks are issued by the pension office. It appears, therefore, that other than pension checks only ten per cent of the Government checks are issued by disbursing officers located here.

Under existing statutes pension checks must be drawn against the Treasurer of the United States and it would not be necessary to transfer to Federal reserve banks other accounts against which checks are drawn for purely local disbursements.

(d) While the bulk of credits for disbursing accounts necessarily originate at Washington, since these are transferred pursuant to appropriations made by Congress, there would be little difficulty in opening such credits with the twelve Federal reserve banks.

(e) The daily and monthly statements could no doubt be prepared with equally as great expedition as under the present system if the balances had to be obtained from the twelve Federal reserve banks and the Treasury Department. Assuming that it is necessary to obtain information by telegram as to the actual balance in the Federal reserve banks this can be done at comparatively small cost, - certainly at much less than the cost of compiling this information under existing circumstances. The statements thus prepared would be more ac-

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curate than is possible under existing circumstances, as it is assumed that the Treasury Department does not obtain a telegraphic report from the seven hundred or more depository banks as to the balances at the end of each day.

(f) The opening of credits with Federal reserve banks for disbursing officers could be arranged with little if any delay.

(g) Information as to balances to the credit of local disbursing officers could be furnished as at present. Disbursing officers located elsewhere could obtain verification of their accounts from the Federal reserve banks in which their accounts are carried.

(h) The greater scrutiny of items made possible under the new system would expedite rather than retard the report of irregularities.

(i) The stop-payment orders would be filed with the Treasurer or with the Federal reserve bank carrying the account by the disbursing officers. It is manifest that such an order could be placed with the Federal reserve bank of San Francisco by a disbursing officer in that district more promptly than is possible with the Treasury Department.

(j) The collection of information for the daily and

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monthly statements should not be delayed under the proposed plan, since it would involve the collection and analysis of twelve accounts rather than the more extensive compilations necessary under the present plan.

Mr. Brown also argued that a decentralization of accounts offers no advantages to offset the disadvantages just considered. In support of this argument he suggests:

(a) That the Government checks are likely to remain outstanding if drawn against Federal reserve banks equally as long as under the present system, since the banks receiving them will still desire to use them for exchange purposes, and since they must be acceptable at par by all depository banks.

(b) That the prompt return of checks is now assured by the requirements that the sixty or more depository banks and the Federal reserve banks remit them directly to the Treasurer; that while this requirement is sometimes disregarded it is more or less effective.

It is evident from these suggestions that the clearing house operations of the Federal reserve banks have been overlooked. A member bank receiving a Government check on a Federal reserve bank bank would have every inducement to for-

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ward it direct to its Federal reserve bank. The credit thus established could be counted as reserve or used for exchange purposes. Under the present system it is understood that when a bank cashes a Government check, if its authorized balance is thereby reduced, arrangements are made to restore this balance as promptly as possible, and the Treasurer will, upon the request of the bank whose balance is depleted, make a deposit for its account with an approved reserve agent. This is no doubt what Mr. Brown means when he says that Government checks can be used to supplement a bank's reserve.

It is obvious, however, that the most direct method of accomplishing this result would be for the member bank to remit the check to its Federal reserve bank where it could be immediately credited to the member bank's reserve account and charged to the account of the disbursing officer whose name appears thereon as a drawer. It would in this way immediately become available as reserve or for exchange purposes, whereas, under the present system the Treasurer's office has to arrange a transfer of funds or a deposit for the account of the member bank remitting the check.

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FOURTH. Contemplated Economies.

Mr. Brown states that the transfer of the accounts to the Federal reserve banks would prevent further important economies in handling the checks which can be effected if the accounts remain in Washington.

The economies contemplated appear to be embodied in a plan by which it will be possible to relieve the Treasurer of the duty of preparing at the end of each month detailed lists of the numbers and amounts of the checks paid for each disbursing officer and instead to permit the Treasurer to turn these checks over to the Auditor daily or weekly with adding machine lists on which the charges against the disbursing officers' accounts were accumulated. It is at once apparent that if this plan is adopted it will be impossible for the disbursing officer to verify his own balance. If neither the checks nor a detailed statement showing the number of the check and the amounts are furnished the disbursing officer, he cannot determine what checks are outstanding and what checks drawn by him have been paid. Mr. Brown states that this improvement has already been applied to the pension account. I am advised, however, that under this plan the pension checks were turned over to the Auditor who was required to prepare and furnish the itemized lists to the disbursing officer,

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so that this merely shifted the work from the office of Treasurer to that of the Auditor, and that as a modification of this plan an arrangement was made by which the Auditor furnishes a list of the unpaid checks in lieu of a list of checks that have been received and paid. If this modified plan were adopted for all accounts it would, of course, be necessary for every disbursing officer to file a duplicate set of accounts with the Auditor of all checks drawn by him so that the Auditor might determine what checks are outstanding at the end of each month.

I am further advised that under the old subtreasury system each assistant Treasurer furnished on the first of each month a detailed list of checks paid, and that there were fewer outstanding checks under this system than the one now in force, for the obvious reason that checks locally drawn were presented to the subtreasuries and cashed promptly, whereas, under the present system they have to be sent to Washington for payment.

Collection of Revenues.

In commenting on the suggestion made in memorandum of July 18 on the subject of collection of revenues, Mr. Brown says:

> "Mr. Elliott's suggestion regarding the handling of Government deposits, namely, that they be received by member banks on behalf of the Federal reserve banks, but that the certificates be transmitted daily to Washington, seems to us excellent. It is not clear, how-

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ever, how this plan will overcome the objection that Mr. Elliott makes to the present system, namely -

(1) That banks accepting checks for credit in the Government's account necessarily assume a certain risk;

(2) That the Division of Public Moneys keeps a large number of acccunts with respect to deposits."

It is true that this plan would not overcome the risk that a bank assumes when it accepts an uncertified check in payment of Government revenues. Under this plan, however, the number of accounts which would be necessary for the Division of Public Moneys to maintain would be reduced from more than 700 to twelve, since the certificates of deposit would be charged against the Federal reserve bank and not the member bank.

Mr. Brown suggests that the accounts in the Division of Public Moneys are probably the so-called journal and register of deposits; that the Bureau of Efficiency deems both unnecessary and has recommended that they should be abolished. That the work of this Division should be limited to checking the totals of certificates of deposit against periodical reports of deposit received from administrative offices. There is evidently a difference of opinion as to the necessity of maintaining this journal and register of deposits. Unless, however,

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the certificates of deposits received are carefully scrutinized and some detailed record is kept, there would seem to be great danger of making credits to the wrong accounts and the necessity for numerous counter entries. The difficulty of tracing items would undoubtedly be increased if ledger entries are made only from adding machine totals. The number of counter entries that have been made as a result of errors discovered through the use of this journal and register will afford a practical demonstration of its value.

In conclusion, it is submitted that the centralization of Government credits and Government disbursements in the office of the Treasurer at Washington is not consistent with the spirit of the Federal Reserve Act. It was the hope of the framers of that Act that Federal reserve bank exchange would gradually replace to a great extent what is commonly called New York exchange, i. e., to say credit balances carried with New York banks.

The congestion of credits in one city necessarily involves constant transfers of funds from and to that city. New York exchange has become one of the most generally used mediums for the settlement of bank balances and the discharge of individual trade and other obligations. A system under which local bank credits can be used in the discharge of local obligations will

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eliminate a great deal of the waste incident to the constant transfer of funds and will reduce the volume of items constantly in transit. The clearing operations carried on by the Federal reserve banks are contributing materially to the accomplishment of the desired objects. The Federal Reserve Board is urging member banks to clear through Federal reserve banks, i. e., to adjust their balances and to make their collections through such banks. The use of these banks as fiscal agents of the Government in the collection and disbursement of its revenues should not only prove a benefit to the Government but will also prove a great benefit to the system by facilitating the settlement of balances without the actual transfer of funds and by increasing the earning capacity of the several Federal reserve banks.

It is, therefore, respectfully submitted that the advantages to be derived more than counterbalance any supposed disadvantages.

Respectfully,

M. C. ELLIOTT.
Counsel.

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AND FISCAL AGENT

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ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 2, 1916.

Dear Mr. Delano :

I send you, herewith, a memorandum, dated October 16, 1916, prepared by Herbert D. Brown, Chief of the United States Bureau of Efficiency, criticizing Mr. Elliott's memorandum dated July 18, 1916, as to the present methods of accounting between the Treasury and depositaries.

Will you kindly read these over. I would suggest that it might be well to make copies of these and send a copy to each Federal Reserve Bank so that they could make a study of the matter and submit suggestions to us. If you approve of this I will ask Mr. Williams for his approval and then we can report it to the Board.

Very truly yours,

C. S. HAMLIN

Hon. F. A. Delano,
Federal Reserve Board.

Enclosures.

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October 16, 1916.

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

Dear Mr. Hamlin :

It recently came to my attention that Mr. Elliott, counsel for the Federal Reserve Board, had submitted a memorandum in which he urged that the revenues of the Government be deposited in Federal reserve banks through their member banks and that the accounts of Government disbursing officers be transferred to the twelve Federal reserve banks under a decentralized system substantially similar to the old subtreasury system. I was also told that Mr. Elliott had supported his proposal with severe criticisms of the present method of keeping disbursing officers' accounts in the Treasurer's office.

As the Bureau of Efficiency was largely responsible for the establishment of the present system in the Treasurer's office, I was naturally interested in the matter, and asked your Secretary for a copy of Mr. Elliott's memorandum in order that I might have the opportunity to judge as to the justice of his criticisms.

An examination of the memorandum revealed several inaccuracies in his description of the Treasurer's system. Moreover, some of the advantages claimed for the transfer of the disbursing officers' accounts to the Federal reserve banks seem to be question-

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able, and certain serious disadvantages of the transfer have been overlooked.

In justice to the Bureasu of Efficiency I feel that I should point out the errors in Mr. Elliott's statements regarding the present system. It also seems desirable that the Federal Reserve Board should be fully advised as to the disadvantages of transferring the disbursing officers' accounts away from Washington, and I am therefore taking the liberty of pointing out some of those disadvantages. I trust that the Board will not regard this as presumptuous.

In a word, we believe that every advantage of the system proposed by Mr. Elliott, and many other advantages, can be obtained by a system under which the disbursing officers' accounts will be kept at Washington. Of Mr. Elliott's criticisms against the routine procedure in the Treasurer's office, none seem important except the statements that the drawer's signature and the last indorsement are not inspected, and that it is difficult to stop payment and to trace items after payment. As explained below, these statements are inaccurate.

While Mr. Elliott criticises the present system on the ground of expense, he offers no specific suggestions as to how the expense could be reduced, and practically every suggestion that he makes regarding methods would increase the expense without substantial benefit.

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The present system in the Treasurer's office was devised after an examination of the systems of several of the largest and most efficient banks in New York. We believe that it will compare favorably in economy and efficiency with the systems of even the most efficient banks, and we respectfully suggest that the Board obtain comparative statistics as to the cost of handling checks in the Treasurer's office and in the Federal reserve banks before adopting the view that the cost of the work in the Treasurer's office is unduly high.

Before the present system was established we also, at your request, gave careful consideration to the question whether the disbursing officers' accounts should be centralized in Washington or distributed among the subtreasuries or Federal reserve banks. At that time we expressed our judgment that the centralization of the disbursing officers' accounts at Washington had important advantages without any serious disadvantages, whether the work were directed and the expense borne by the United States or by the Federal reserve banks.

This belief was based on the fact that the majority of the officers who have occasion to consult the accounts, or to be consulted with respect to them, are located here in Washington. Practically all of the administrative officers who have supervision over the disbursing officer's work are stationed in Washington. About 60 per cent of all the checks are issued in Washington. The bulk of the credits

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originate in Washington through action taken by the Secretary of the Treasury on the request of the heads of the executive departments. The controlling accounts from which are drawn the daily and monthly statements of the condition of the Treasury are kept in Washington. Keeping the disbursing officers' accounts elsewhere would delay the entry of credits to disbursing officers, the furnishing of information regarding balances on requests by administrative and disbursing officers, the reporting of irregularities to administrative officers, the filing of the majority of the notices to stop payment, and the gathering of information for the daily and monthly statements of the condition of the Treasury. It would make necessary the use of the telegraph in hundreds of cases where telephone or messengers are now used.

The decentralization of the accounts seems to have no advantage to offset the foregoing disadvantages. The chief objection to centralization that is urged by Mr. Elliott, namely, that the checks are likely to remain outstanding a long time because they can be conveniently used by banks to establish credit and settle balances in other cities, would apply with equal force to any system under which Government checks could be cashed at par in any part of the United States. If the system urged by Mr. Elliott does not meet this requirement it would certainly be unsatisfactory. If it does meet this requirement it would not prevent the checks from

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being used in establishing credit and settling balances between different cities and would not expedite their return to the office on which they were drawn.

At present the reasonably prompt return of the checks to Washington is assured by the requirement that each of the 60, or more depositary banks, including the Federal reserve banks, must remit directly to the Treasurer all Government checks received by them. While this requirement is sometimes disregarded, it is on the whole effective, and the checks apparently do not stay out much, if any, longer than under the old subtreasury system.

It is true that under the present system many Government checks are handled in Federal reserve banks and again handled in the Treasurer's office, and it would seem that a saving could be effected by allowing such checks to be finally paid and charged to the drawers' accounts in the Federal reserve banks. In fact, however, this would not be the most satisfactory method of eliminating the duplication, for three reasons :

(1) It would not be effective unless many of the disbursing officers maintained several accounts and drew every check on the Federal reserve bank in whose district the payee resided. This would impose considerable additional labor and expense on disbursing officers, and would necessitate their holding, in the aggregate, larger balances.

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(2) The same result can be obtained even more effectively by retaining the accounts at Washington and having the member banks send Government checks directly to Washington for credit in their reserve accounts at their Federal reserve banks.

(3) The transfer of the accounts to the Federal reserve banks would prevent further important economies in the handling of the checks that can be effected if the accounts remain in Washington.

These points are discussed below in greater detail:

(1) Mr. Elliott suggests that each disbursing officer keep his account in the Federal reserve bank in whose district he is stationed. Under this plan it is probable that as many Government checks would be handled by two Federal reserve banks as are now handled by one Federal reserve bank and the Treasurer's office. Take, for example, the 60 per cent of all disbursing officers' checks that are drawn in Washington. These checks are payable in all parts of the United States. Only a comparatively small number are paid in the Richmond district. If they were all drawn on the Richmond bank, a large majority would be paid in other Federal reserve districts and sent through the reserve banks of those districts to the Richmond bank, just as they are now sent to the Treasurer. In fact, a large percentage of them would probably be doubly handled in this way, for under the present plan many of the checks do not pass through the Federal reserve banks, but come directly to the Treasurer from member banks, whereas under

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the proposed plan, as we understand it, all exchanges between districts would be made through the Federal reserve banks.

At Richmond the accounts would be located inconveniently for the drawers, the administrative officers, and the Treasury officials. They would be convenient to no one.

If, on the other hand, an effort were made to draw all checks on the Federal reserve banks in whose districts the payees resided, it would be necessary for many disbursing officers to have a number of accounts where they now maintain one. As can be easily seen, this would add to the labor of granting credits, drawing checks, looking up checks on subsequent inquiries (especially if the payee's address should not be known), and assembling checks with vouchers in the auditors' offices. Under such a plan none of the accounts maintained by Washington disbursing officers would be convenient for reference by any Government officer.

(2) Turning to the second point, it would be quite simple to apply to check payments substantially the same plan that Mr. Elliott indorses for Government deposits - that is, to permit member banks to pay checks on behalf of their Federal reserve banks, but require them to remit the paid checks directly to Washington. Under this plan the member banks by paying Government checks and sending them to Washington, could replenish their reserve deposits. This

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would give them a strong incentive to retire Government checks, rather than send them to some other bank. In order that the credits might be entered promptly on the books of the Federal reserve banks, duplicate transit letters should be sent to those banks. The totals of these letters should be credited to the member banks and charged to the Government promptly, subject, however, to verification from Washington.

This plan would go as far as possible in eliminating duplication in the handling of Government checks, and at the same time would retain the accounts at Washington and give the Federal reserve banks the advantage of all the Government deposits that are maintained for the payment of Government checks.

(3) Under the present plan we believe that it will be possible to relieve the Treasurer of the duty of preparing at the end of each month detailed lists of the numbers and amounts of the checks paid for each disbursing officer, and instead permit him to turn the checks over to the auditor daily or weekly with the adding machine lists on which the charges against the disbursing officers' accounts were accumulated. This plan, which would hardly be practicable if the disbursing officers' accounts were kept away from Washington, would also facilitate a prompt audit of paid vouchers, which we believe will become possible in the near future. This improvement has already been applied to the largest account - that of the pension disbursing officer, who issues nearly one-half of all Government checks. If the pension account were distributed among the reserve banks or transferred to Richmond, it would be necessary to resume

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the practice of listing the paid checks, at large expense, and also to delay the audit at least a month.

The argument urged by Mr. Elliott in favor of the proposed system, that it would make the funds of the United States available in the parts of the country where they are most needed and that it would make the deposits of revenues available for the payment of checks without the physical transfer of money, is equally applicable to the present system, which was adopted for the purpose of securing those very advantages. Depositary banks are now selected with regard to convenience in depositing Government revenues and paying Government checks, and the balances in the several depositaries are determined by the need for Government funds in the locality. Each depositary pays the Government checks presented to it out of the Government revenues deposited with it, and settles with the most convenient subtreasury or depositary bank for the net excess or deficiency of receipts only. Usually the settlement is made by check or draft. The points to which the transfers are made are subject to the control of the Treasury Department, which has a complete record of the daily balances in every bank.

Mr. Elliott's suggestion regarding the handling of Government deposits - namely, that they be received by member banks on behalf of the Federal reserve banks, but that the certificates

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be transmitted daily to Washington - seems to us excellent. It is not clear, however, how this plan would overcome the objections that Mr. Elliott makes to the present system, namely, (1) that banks accepting checks for credit in the Government's account necessarily assume a certain risk, and (2) that the Division of Public Moneys keeps a large number of accounts with respect to deposits.

(1) The risk in accepting checks for credit in the Government's account would seem to be the same whether the receiving bank takes the deposits on its own behalf or on behalf of its Federal reserve bank.

(2) It is presumed that in speaking of the accounts in the Division of Public Moneys, Mr. Elliott refers to the so-called covering journal and register of deposits. On January 10, 1916, we pointed out, in a memorandum to the Assistant Secretary of the Treasury, that this journal and register are wholly unnecessary under the present system and that a saving of more than $20,000 a year can be effected by discontinuing these records and limiting the work of the Division of Public Moneys to that of checking the totals of certificates of deposit against periodic reports of deposits received from administrative offices.

In order that the deposits may be properly credited we believe that it will be necessary for the Treasury to get such

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reports of deposits from administrative offices rather than depend on the accounts current of the Federal reserve banks, as Mr. Elliott apparently intends to suggest; for the Federal reserve banks' information as to the source of the money deposited would not be reliable enough to be depended on as the basis for final entries in the Treasury books.

Turning to Mr. Elliott's criticisms of the routine procedure in the Treasurer's office we find them to be (1) that the checks are not properly scrutinized before payment; and (2) that stoppage of payment on checks and tracing of items after payment is difficult.

(1) Mr. Elliott states that the Treasurer's office does not give proper scrutiny to (a) the drawer's signature, (b) the last indorsement, (c) the original indorsement, (d) intermediate indorsements in order, and (e) the object for which drawn.

(a) In fact, the method of verifying the drawer's signature in the Treasurer's office is more effective than the usual method in banks. The checks are sorted by account numbers behind guide cards bearing the autograph signatures of the disbursing officers and of any deputies authorized to sign in their places, and the correctness of the sorting is verified by a careful visual comparison of the signatures on the checks with the autograph signatures on the guides. Under this system, I understand that no

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forgery or unauthorized signature has slipped through that could have been detected except by a handwriting expert after careful study.

(b) The last indorsements on the checks are not examined in the Treasurer's office but the checks are perforated in such a manner as to connect them unfailingly with the banks' transcripts of account on which they are listed. I understand that in two years of operation, during which nearly 20,000,000 checks have been handled, there has not been a case of inability to trace a check back to the last indorser, although thousands of checks have been returned to the banks transmitting them.

(c) The original indorsement is not examined because in our judgment and in that of the Treasurer such an examination would merely waste the Government's money. The most that the examination could show is that the check was indorsed in the same name in which it was drawn. If a fraud had been attempted the check would almost infallibly be so indorsed, while if the right person had received payment, but had indorsed the check erroneously, the detection of that fact in the Treasurer's office would merely lead to fruitless labor. We understand that in the two years during which the present system has been in

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operation there has been no loss that an inspection of the original indorsement would have prevented and no error that such an inspection of the original indorsement would have prevented and no error that such an inspection would have detected. On the other hand it is estimated by the Treasurer's office that in the two years the work of inspection would have cost not less than $10,000.

If an examination of the original indorsement is desirable it could be made much more effectively by the Auditor than by the Treasurer, for the Auditor could compare the indorsement with the payee's signature on the voucher and might thus detect a forgery, while the Treasurer could detect nothing but a misspelling or a failure of the payee to indorse.

If anything should be wrong with the indorsement of a check all the banks indorsing the check would be liable, since all of them have guaranteed prior indorsements; and the Treasurer is in a position to send the check back to the last indorser, on whom the burden of holding the prior indorsers would rest.

(d) The Treasurer does not inspect intermediate indorsements nor see that they are in order. While we are not familiar with the methods of all the large banks in the coun-

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try, we doubt if any of them puts itself to such a needless expense.

(e) The statements on the checks as to the object for which they are drawn are also not verified. This does not concern the Treasurer any more than the object for which personal checks are drawn concerns the bank that pays them. If the Treasurer should examine these statements he would have no means of verifying them, since he does not have the vouchers. Even if he should detect that the object for which drawn was erroneously stated, there would be nothing that he could do about it with advantage. The purpose for which a check was drawn is a question for the consideration of the Auditor, who has the voucher that was paid thereby.

(2) We are at a loss to know the basis for Mr. Elliott's statement that it is unusually difficult to stop payment on checks under the present system in the Treasurer's office. Every day, after the checks chargeable in each disbursing officer's account have been listed to obtain the amount to be charged to his account, the checks are sorted according to the thousands digit of the serial number, and a search is made in each thousand for checks on which stop orders have been issued, as shown by a list prepared for the pur-

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pose. I understand that very few checks escape this search - probably not more than would escape the bookkeeper in a bank in which checks were posted individually to the account of the drawer.

During the two years that the present system has been in operation in the Treasurer's office I understand that no serious difficulty has arisen in tracing items after payment. It is true that, for the sake of economy, receipts and payments are entered on the books of the Treasurer's office in totals, and that the totals are obtained from adding machine lists of the amounts only, without descriptive entries; so that an item can be traced into the ledgers through the adding machine lists only by its amount. However, two descriptive entries of each item are retained in the Treasurer's office or in some other office of the Treasury Department where they are easily available: (a) The entry on the transcript of the bank that received the deposit or paid the check, and (b) The deposit slip or check itself, which is filed according to the account to which it was posted. When a deposit slip or check leaves the Treasury Building it is recorded in detail so that it can be easily traced.

Very respectfully,

HERBERT D. BROWN
Chief, Bureau of Efficiency.

12/15/16

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December 14, 1916.

PRESS STATEMENT.

A conference of the Governors of Federal Reserve Banks was held at the Shoreham Hotel Washington, D. C., December 11th to 14th, inclusive. There were present, A. L. Aiken, Governor of the Federal Reserve Bank of Boston, Governor G. J. Seay, of Richmond, Governor C. J. Rhoads, of Philadelphia, Governor Rollo Wells, of St. Louis, Governor Theo. Wold, of Minneapolis, Governor J. A. McCord, of Atlanta, Vice Governor R. H. Treman, of New York, Governor J. Z. Miller, of Kansas City, Governor R. L. Van Zandt, of Dallas, Governor E. R. Fancher, of Cleveland, Governor J. B. McDougal, of Chicago, Mr. J.F.Curtis, Counsel of the Federal Reserve Bank of New York and Secretary to the Conference; also Mr. Marcus Walker, Manager of the New Orleans branch of the Federal Reserve Bank of Atlanta, Mr. L. H. Hendricks, Assistant Cashier of the Bank of New York, Mr. C. C. Bullen, Auditor of the Federal Reserve Bank of Boston and Mr. A. H. Hale, Auditor of the Federal Reserve Bank of St.Louis.

The Governors held several meetings with the Federal Reserve Board and with various committees of the Board , at which topics connected with the administration of the banks were taken up for discussion and recommendations made.

Among the subjects considered were the following:

Reserve and central reserve cities, disposition of Government bonds, Reserve banks as fiscal agents of the Government, uniformity in reports of reserves and enforcement of reserve penalties, report of the transit managers' conference held at Chicago, report of the auditors meeting held at Chicago, handling of gold settlement fund, retirement of National bank notes, vault

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reserves, purchase of domestic and foreign acceptances, conversion of three per cent Treasury notes into thirty-year three per cent bonds, treatment of organization expenses, collections and clearances, loans on farm land and other real estate, National banks as insurance agencies, the accumulation of gold by Federal reserve banks, and the establishment of branches or agencies of Federal reserve banks.

The conference adjourned to meet subject to call without any definite time or place for the next meeting.

12/14/16

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

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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

920 ADDRESS REPLY TO
FEDERAL RESERVE BOARD

In December 1914, the Federal Reserve Board held an examination of applicants for appointment to its staff. As the result of this examination there was established an eligible list for stenographers and typewriters, typewriters only, stenographers only, clerks, bookkeepers and messengers. So few appointments were made from the list that the Board extended it through 1916.

Your name appears on the list as having passed the examination for the grade checked above. While no appointments are at present contemplated, this letter is written to ask if you desire to remain upon the eligible list, and if so, that you will return this letter indicating such desire and the minimum salary which you would accept should you be offered an appointment during the year 1917. There is inclosed a franked envelope for your reply.

Respectfully,

Secretary.

I {do / do not} desire to remain on the list.

I will accept appointment at $ per annum.

Inclosure.

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WASHINGTON

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

December 18, 1916.

Dear Sir:

On December 28, 1915, the Board adopted a resolution regarding membership in the Federal Advisory Council which appears on page 3 of the January, 1916, issue of the Federal Reserve Bulletin.

Inquiries have been received from Federal Reserve Agents asking for definite advice as to whether Federal Reserve bank directors should be voted for as members of the Federal Advisory Council. The Board is of the opinion that while it is desirable that officers of Federal reserve banks, whose salaries are approved by the Board, should not serve on the Advisory Council, there is no reason at this time to seek to impose such a limitation upon any director of any Federal reserve bank. While it may be to the advantage of the system that there should be rotation in memberships on the Advisory Council, it is nevertheless desirable that changes be so made that a majority of the membership may not be made up of new men.

The matter will be taken up with the Advisory Council at its next meeting with the view of having the Council itself recommend to the Federal Reserve Banks a well considered plan for rotation in its membership. The Board desires, as far as the forthcoming election is concerned, that Class "C" directors feel free to exercise their own judgment.

Very truly yours,

Governor.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That clause "m" of Section 11 of the Act approved December 23, 1913, as amended by the Act of September 7, 1916, be and it is hereby amended so as to read as follows:

> "Upon the affirmative vote of not less than five of its members the Federal Reserve Board shall have power, from time to time, by general ruling, covering all districts alike, to permit member banks -
>
> (1) To carry in the Federal reserve banks of their respective districts any portion of their reserves now required by section nineteen of this Act to be held in their own vaults.
>
> (2) TO COUNT AS PART OF THEIR LAWFUL RESERVES FEDERAL RESERVE NOTES OF THEIR OWN DISTRICT NOT EXCEEDING IN THE AGGREGATE AN AMOUNT EQUAL TO FIVE PER CENTUM OF THEIR NET DEMAND DEPOSITS.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That the first paragraph of Section 13 of the Act approved December 23, 1913, as amended by the Act of September 7, 1916, be further amended so as to read 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 payable upon presentation, and also for collection, maturing bills; or, solely for purposes of exchange or of collection, may receive from other Federal reserve banks OR FROM NON-MEMBER BANKS OR TRUST COMPANIES deposits of current funds in lawful money, national bank notes, or checks AND DRAFTS upon SOLVENT BANKS OR TRUST COMPANIES OR other Federal reserve banks ~~and checks and drafts~~ payable upon presentation within its district and maturing bills payable within its district; PROVIDED, HOWEVER, THAT NO FEDERAL RESERVE BANK SHALL RECEIVE CHECKS AND DRAFTS FROM A NON-MEMBER BANK FOR THE PURPOSE OF EXCHANGE OR COLLECTION UNLESS SUCH NON-MEMBER BANK MAINTAINS WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT A BALANCE IN AN AMOUNT TO BE DETERMINED BY THE FEDERAL RESERVE BOARD UNDER SUCH RULES AND REGULATIONS AS IT MAY PRESCRIBE, BUT SUCH BALANCE SHALL IN NO EVENT BE LESS THAN FIFTY PER CENTUM NOR GREATER THAN ONE HUNDRED PER CENTUM OF THE AMOUNT OF BALANCES REQUIRED TO BE MAINTAINED BY MEMBER BANKS LOCATED IN THE SAME PLACE AS SUCH NON-MEMBER BANK.

12-19-16.

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BRANCH BANKS

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 25 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act of September 7, 1916, be amended by adding a sub-section (a) to read as follows:

"Sec. 25a. That any member bank located in a city or incorporated town of more than one hundred thousand inhabitants and possessing a capital and surplus of $1,000,000 or more may, under such rules and regulations as the Federal Reserve Board may prescribe, establish branches, not to exceed ten in number, within the corporate limits of the city or town in which it is located; Provided, That no such branch shall be established in any State in which neither State banks nor trust companies may lawfully establish branches."

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COMPTROLLER OF THE CURRENCY

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CHARLES S. HAMLIN

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

ADDRESS REPLY TO
929 FEDERAL RESERVE BOARD

December 20, 1916.

Dear Sir:

Much to its surprise, the Federal Reserve Board has learned that there are Federal reserve agents and governors of Federal reserve banks who have overlooked or failed to receive "Special Instructions No. 2 of 1916," dated September 15, 1916, ten copies of which were sent to each Federal reserve agent at the time of issue.

These instructions were also printed on Page 529 of the Federal Reserve Bulletin for October.

There are inclosed herewith copies of the Special Instructions for your information and guidance in case they have escaped your attention.

Very truly yours,

Secretary.

Inclosures.

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Whereas it appears that the 12 Federal reserve banks have purchased in the open market bonds in excess of the amount which might have been allotted to such banks at the end of this quarterly period on the basis heretofore determined upon and announced by the Board: Now, therefore, be it

RESOLVED, That it is the sense of the Board that no necessity exists for enforcing the requirement provided for under section 18 of the Federal Reserve Act at the end of this quarterly period ending December 31, 1916, and that it will not, therefore, at this time require the Federal reserve banks to purchase any of the bonds which are offered for sale by member banks through the Treasurer of the United States under the provisions of section 18: Be it further

RESOLVED, That the Secretary be instructed to send a copy of this resolution to the various Federal reserve banks and to the member banks which have offered bonds for sale in order that they may be notified of the action of the Board in the premises.

December 27, 1916.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

933.

December 28, 1916.

Dear Sir:

There is inclosed for your information and guidance copy of a resolution adopted by the Federal Reserve Board on Wednesday, December 27, to the effect that since Federal reserve banks have purchased all of the United States 2% bonds which they can be required to take in this calendar year, no purchases will be required under Section 18 of bonds offered by member banks through the Treasurer of the United States at the close of this quarterly period.

For your confidential information, and that you may, if you desire, offer to purchase the bonds offered, there is given in the lower left-hand corner of this sheet the names of the banks offering bonds in your District and the amounts thereof.

Very truly yours,

Secretary.

Inclosure.

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ADDRESS REPLY TO
934 FEDERAL RESERVE BOARD

December 23, 1916.

Dear Sir:

With reference to Form 34 (1917 edition) copies of which will be sent to you from the Government Printing Office, the following observations may prove useful:

1. Items BALE and BANK in the first block should be given net - i. e., less amounts of paper rediscounted with other Federal reserve banks, but including amounts pledged with the Federal reserve agent. Item BALE is to comprise all paper discounted for member banks, including trade acceptances (two-name paper) discounted, also commodity paper. Trade acceptances based upon foreign trade, as well as domestic trade transactions when purchased in the open market, should be shown together with bankers' acceptances in item BEND.

11. Item BITE is to include the amounts of U. S. bonds held by the bank itself, as well as amounts held in suspense account with the Secretary of the Treasury.

111. Item "Expense Current" is to show the segregated expense of the bank proper; disbursements of transit department are to be shown in the following subdivision.

The Board is of the opinion that the headings "Deferred Debits" and "Deferred Credits" printed in the draft improperly describe the items grouped thereunder. Accordingly the headings have been changed to read "Collection Items - Debits" and "Collection Items - Credits", and the items themselves have been moved to the next subdivision, to follow item BULB ("Checks and Other Cash Items") and CALK ("Federal Reserve Bank drafts") on the asset and liability sides respectively. TALK ("Total deferred debits") and TANK ("Total deferred credits") printed in the draft have like-

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wise been eliminated. It is the desire of the Board that the banks, as soon as practicable, change their account forms so as to be able to furnish the Board with daily figures against all items in the deposit block and against corresponding items on the resource side of Form 34.

Item "Service charges - net" represents the difference between the amounts of service charges against member banks and other Federal reserve banks collected or accrued and the amounts of service charges paid or payable to other Federal reserve banks.

Item "Paper pledged with Agent (DRAB) is a memorandum account and should not be combined with the other liabilities shown on the form. No offsetting entry need be made on the asset side of Form 34.

The net liability on Federal reserve notes is to be figured by deducting from the amount of Federal reserve notes outstanding (Item DEER) the amounts of gold and lawful money deposited with the Federal reserve agent (Item DOPE) and should therefore equal item COKE. Amounts of Federal reserve notes in the hands of the Federal reserve bank should not be deducted.

Respectfully,

Secretary.

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

936

December 26, 1916.

I am glad to inform you that acting upon a report of the Committee on Organization, Expenditures and Staff, submitted on December 23, 1916, the Federal Reserve Board has increased your salary by $10 per month, effective January 1, 1917.

Very truly yours,

Secretary.

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STATEMENT FOR THE PRESS.

December 25, 1916.

The Federal Reserve Board has authorized the Federal Reserve Bank of New York to appoint as one of its foreign correspondents and agents the Bank of England of London, England, under the terms of the Federal Reserve Act.

Section fourteen of the Act permits any Federal reserve bank "with the consent of the Federal Reserve Board to open and maintain banking accounts in foreign countries, appoint correspondents and establish agencies in such countries wheresoever it may deem best for the purpose of purchasing selling and collecting bills of exchange and to buy and sell with or without its indorsement through such correspondents or agencies bills of exchange arising out of actual commercial transactions" so that a broad field of operations is possible under it.

In granting the authority to establish this agency the Board has authorized the Federal Reserve Bank of New York to maintain accounts either with or for the Bank of England so that operations both in England and in the United States are possible.

Other Federal reserve banks may participate in the agency relationship with the Bank of England upon the same terms and conditions that will govern the Federal Reserve Bank of New York, if they so desire.

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M E M O R A N D U M .

December 27, 1916.

Attention is again called to the direction of the Board that where letters written to Federal Reserve agents contain matter affecting the operation of the bank and of direct interest to the Governors of Federal Reserve banks copy of the letter be marked "For the Bank" and sent to it. The same procedure is to be followed where letters are written to the banks which affect or interest the Federal Reserve agents.

It is directed that hereafter the words "Copy sent to bank" or "Copy sent to Federal Reserve Agent" be written on the original letter and thus on through the carbon sheets. The office carbon then will show that a copy has been sent.

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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

941

December 28, 1916.

Dear Sir:

We are advised by some of the Federal reserve agents that their supply of Form F.R.A. - 5 is nearing exhaustion and we are proposing, therefore, to place an order with the Government Printing Office for a new supply of this form. Please let us know at your earliest convenience whether the form in its present shape is fully satisfactory, and if not, what changes you have to recommend in it.

Kindly state also how many copies of the form you will desire for your needs in the coming year.

Respectfully,

Secretary.

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AMENDMENTS PROPOSED BY THE

FEDERAL RESERVE BOARD

in the form approved by the Board on

December 20, 1916.

1/2/17

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That section sixteen, paragraphs two, three, four, five, six and seven, of the Act approved December twenty-third, nineteen hundred and thirteen, known as the Federal Reserve Act, as amended by the Act of September 7, 1916, be further amended and re-enacted so as to read as follows:

"Any Federal reserve bank may make application to the local Federal reserve agent for such amount of the Federal reserve notes hereinbefore provided for as it may require. Such application shall be accompanied with a tender to the local Federal reserve agent of collateral in amount equal to the sum of the Federal reserve notes thus applied for and issued pursuant to such application. The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances rediscounted under the provisions of Section thirteen of this Act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of Section fourteen of this Act, or bankers' acceptances purchased under the provisions of said section fourteen; OR GOLD OR GOLD CERTIFICATES; BUT IN NO EVENT SHALL SUCH COLLATERAL SECURITY WHETHER GOLD, GOLD CERTIFICATES, OR ELIGIBLE PAPER, BE LESS THAN THE AMOUNT OF FEDERAL RESERVE NOTES APPLIED FOR. The Federal reserve agent shall each day notify the Federal Reserve Board of all issues and withdrawals of Federal reserve notes to and by the Federal reserve bank to which he is accredited. The said Federal Reserve Board may at any time call upon a Federal reserve bank for additional security to protect the Federal reserve notes issued to it.

"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. PROVIDED, HOWEVER THAT WHEN THE FEDERAL RESERVE AGENT HOLDS GOLD OR GOLD CERTIFICATES AS COLLATERAL FOR FEDERAL RESERVE NOTES ISSUED TO THE BANK SUCH GOLD OR GOLD CERTIFICATES SHALL BE COUNTED AS PART OF THE GOLD RESERVE WHICH SUCH BANK IS REQUIRED TO MAINTAIN AGAINST ITS FEDERAL RESERVE NOTES IN ACTUAL CIRCULATION ~~and not offset by gold or lawful money deposited with the Federal reserve agent~~. Notes so paid out shall bear upon their faces a distinctive letter and serial number, which shall be assigned by the Federal Reserve Board to each Federal reserve bank. Whenever Federal reserve notes issued through one Federal reserve bank shall be received by another Federal reserve bank they shall be promptly returned for credit or redemption to the Federal reserve bank through which they were originally issued, OR, UPON DIRECTION OF SUCH FEDERAL RESERVE BANK THEY SHALL BE FORWARDED DIRECT TO THE TREASURER OF THE UNITED STATES TO BE RETIRED. No Federal reserve bank shall pay out notes issued through another under penalty of a tax of ten per centum upon the face value of notes so paid out. Notes presented for redemption at the Treasury of the United States shall be paid out of the redemption fund and returned to the Federal reserve banks through which they were originally issued, and thereupon such Federal reserve bank shall, upon demand of the Secretary of the Treasury, reimburse such redemption fund in lawful money, or, if such Federal reserve notes have

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been redeemed by the Treasurer in gold or gold certificates, then such funds shall be reimbursed to the extent deemed necessary by the Secretary of the Treasury in gold or gold certificates, and such Federal reserve banks shall, so long as any of its Federal reserve notes remain outstanding, maintain with the Treasurer in gold an amount sufficient in the judgment of the Secretary to provide for all redemptions to be made by the Treasurer. Federal reserve notes received by the Treasurer, otherwise than for redemption, may be exchanged for gold out of the redemption fund hereinafter provided and returned to the reserve bank through which they were originally issued, or ~~they~~ may be returned to such bank for the credit of the United States. Federal reserve notes unfit for circulation shall be returned by the Federal reserve agents to the Comptroller of the Currency for cancellation and destruction.

"The Federal Reserve Board shall require each Federal reserve bank to maintain on deposit in the Treasury of the United States a sum in gold sufficient in the judgment of the Secretary of the Treasury for the redemption of the Federal reserve notes issued to such bank, but in no event less than five percentum OF THE TOTAL AMOUNT OF NOTES ISSUED LESS THE AMOUNT OF GOLD OR GOLD CERTIFICATES HELD BY THE FEDERAL RESERVE AGENT AS COLLATERAL SECURITY; but such deposit of gold shall be counted and included as part of the forty percentum reserve hereinbefore required. The Board shall have the right, acting through the Federal reserve agent, to grant in whole or in part or to reject entirely the application of any Federal reserve bank for Federal reserve notes; but to the extent that such application may be granted the Federal Reserve Board shall, through its local Federal reserve agent, supply Federal reserve notes to the bank so applying, and such bank shall be charged with the amount of notes ISSUED TO IT and shall pay such rate of interest ~~on said amount~~ as may be established by the Federal Reserve Board ~~and the amount of~~ ON ONLY THAT AMOUNT OF SUCH NOTES WHICH EQUALS THE TOTAL AMOUNT OF ITS OUTSTANDING FEDERAL RESERVE NOTES LESS THE AMOUNT OF GOLD OR GOLD CERTIFICATES HELD BY THE FEDERAL RESERVE AGENT AS COLLATERAL SECURITY. Federal reserve notes ~~as~~ issued to any such bank shall, upon delivery, together with such notes of such Federal reserve bank as may be issued under section eighteen of this Act upon security of United States two percentum Government bonds, become a first and paramount lien on all the assets of such bank.

~~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~~

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~~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 the paid gold~~ to the Treasurer of the United States SO MUCH OF THE GOLD HELD BY HIM AS COLLATERAL SECURITY FOR FEDERAL RESERVE NOTES as may be required for the exclusive purpose of the redemption of of such ~~notes~~ FEDERAL RESERVE NOTES BUT SUCH GOLD WHEN DEPOSITED WITH THE TREASURER SHALL BE COUNTED AND CONSIDERED AS IF COLLATERAL SECURITY ON DEPOSIT WITH THE FEDERAL RESERVE AGENT.

Any Federal reserve bank may at its discretion withdraw collateral deposited with the local Federal reserve agent for the protection of its Federal reserve notes ~~deposited with it~~ ISSUED TO IT and shall at the same time substitute therefor other ~~like~~ collateral of equal amount with the approval of the Federal reserve agent under regulations to be prescribed by the Federal Reserve Board. ANY FEDERAL RESERVE BANK MAY RETIRE ANY OF ITS FEDERAL RESERVE NOTES BY DEPOSITING THEM WITH THE FEDERAL RESERVE AGENT OR WITH THE TREASURER OF THE UNITED STATES, AND SUCH FEDERAL RESERVE BANK SHALL THEREUPON BE ENTITLED TO RECEIVE BACK THE COLLATERAL DEPOSITED WITH THE FEDERAL RESERVE AGENT FOR THE SECURITY OF SUCH NOTES. FEDERAL RESERVE BANKS SHALL NOT BE REQUIRED TO MAINTAIN THE RESERVE OR THE REDEMPTION FUND HERETOFORE PROVIDED FOR AGAINST FEDERAL RESERVE NOTES WHICH HAVE BEEN RETIRED; NOR SHALL THEY BE FURTHER LIABLE TO PAY ANY INTEREST CHARGE WHICH MAY HAVE BEEN IMPOSED THEREON BY THE FEDERAL RESERVE BOARD. FEDERAL RESERVE NOTES SO DEPOSITED SHALL NOT BE REISSUED EXCEPT UPON COMPLIANCE WITH THE CONDITIONS OF AN ORIGINAL ISSUE.

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AMENDMENT OF SECTION 19 - R E S E R V E S.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 19 of the Act approved December 23, 1913, amended by an Act of August 14, 1914, be further amended and re-enacted so as to read as follows:

Sec. 19. 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 deposit which are subject to not less than thirty days' notice before payment, AND ALL POSTAL SAVINGS DEPOSITS.

~~When the Secretary of the Treasury shall have officially announced, in such manner as he may elect, the establishment of a Federal reserve bank in any district, every subscribing member~~ EVERY bank, BANKING ASSOCIATION, OR TRUST COMPANY WHICH IS OR WHICH BECOMES A MEMBER OF ANY FEDERAL RESERVE BANK shall establish and maintain RESERVE BALANCES WITH ITS FEDERAL RESERVE BANK ~~reserves~~ as follows:

(a) IF a ~~bank~~ not in a reserve or central reserve city as now or hereafter defined, it shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT AN ACTUAL NET BALANCE ~~reserves~~ equal to NOT LESS THAN ~~twelve~~ SEVEN per centum of the aggregate amount of its demand deposits and ~~five~~ THREE per centum of its time deposits, ~~as follows:~~

~~In its vaults for a period of thirty-six months after said date five-twelfths thereof and permanently thereafter four twelfths.~~

~~In the Federal reserve bank of its district, for a period of twelve months after said date, two-twelfths, and for each succeeding six months an additional one-twelfth, until five twelfths have been so deposited, which shall be the amount permanently required.~~

~~For a period of thirty-six months after said date the balance of the reserve may be held in its own vaults, or in the Federal reserve bank, - or in national banks in reserve or central reserve cities as now defined by law.~~

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After said thirty-six months' period, said reserves, other than those hereinbefore required to be held in the vaults of the member bank and in the Federal reserve bank, shall be held in the vaults of the member bank or in the Federal reserve bank or in both, at the option of the member bank.

(b) IF a bank in a reserve city, as now or hereafter defined, it shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT AN ACTUAL NET BALANCE reserves equal to NOT LESS THAN fifteen TEN per centum of the aggregate amount of its demand deposits and five THREE percentum of its time deposits, as follows:

In its vaults for a period of thirty-six months after said date six fifteenths thereof, and permanently thereafter five fifteenths.

In the Federal reserve bank of its district for a period of twelve months after the date aforesaid at least three fifteenths, and for each succeeding six months an additional one fifteenth, until six fifteenths have been so deposited, which shall be the amount permanently required.

For a period of thirty-six months after said date the balance of the reserves may be held in its own vaults, or in the Federal reserve bank, or in national banks in reserve or central reserve cities as now defined by law.

After said thirty six months' period all of said reserves except those hereinbefore required to be held permanently in the vaults of the member bank and in the Federal reserve bank, shall be held in the vaults of the Federal reserve bank, or in both. at the option of the member bank.

(c) IF a bank in a central reserve city, as now or hereafter defined IT shall hold and maintain WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT AN ACTUAL NET BALANCE reserve equal to NOT LESS THAN eighteen THIRTEEN per centum of the aggregate amount of its demand deposits and five THREE per centum of its time deposits as follows:

In its vaults six-eighteenths thereof.
In the Federal reserve bank seven-eighteenths.
The balance of said reserves shall be held in its own vaults or in the Federal reserve bank at its option.

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EVERY MEMBER BANK SHALL MAINTAIN IN ITS OWN VAULTS FOR TILL MONEY AN AMOUNT OF SPECIE OR CURRENCY EQUAL TO AT LEAST FIVE PER CENTUM OF ITS DEMAND DEPOSITS LESS THE AMOUNT OF THOSE BALANCES WITH THE FEDERAL RESERVE BANK WHICH ARE IN EXCESS OF THE MINIMUM BALANCES REQUIRED BY THIS SECTION.

~~Any Federal reserve bank may receive from the member banks as reserves, not exceeding one-half of each instalment, eligible paper as described in section fourteen, properly indorsed and acceptable to the said reserve bank.~~

~~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~~ No member bank shall keep on deposit with any nonmember bank a sum in excess of ten per centum of its own paid-up capital and surplus. No member bank shall act as a medium or agent of a nonmember 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.

The REQUIRED BALANCE ~~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~~ BALANCE required by law is fully restored.

In establishing the ~~reserves~~ BALANCES required by this Act, the net DIFFERENCE ~~balance~~ of amounts due to and from other banks shall be taken as the basis for ascertaining the deposits against which ~~reserves~~ REQUIRED BALANCES WITH FEDERAL RESERVE BANKS shall be determined. ~~Balances in reserve banks due to member banks shall to the extent herein provided, be counted as reserves.~~

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National banks, OR BANKS ORGANIZED UNDER LOCAL LAWS, located in Alaska or IN A DEPENDENCY OR INSULAR POSSESSION OR ANY PART OF THE UNITED STATES outside the continental United States may remain nonmember banks, and shall in that event maintain reserves and comply with all the conditions now provided by law regulating them; or said banks ~~except in the Philippine Islands~~ may, with the consent of the Federal Reserve Board become member banks of any one of the reserve districts, and shall, in that event, take stock, maintain reserves and be subject to all the other provisions of this Act.

THIS ACT SHALL BECOME EFFECTIVE SIXTY DAYS AFTER ITS PASSAGE.

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AMENDMENT TO SECTION 11 (c).

INCREASE OF RESERVES.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That clause (c) of Section 11 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act approved September 7, 1916, be and is hereby amended by adding at the end thereof the following sentence;

> "The Federal Reserve Board shall also have power, whenever extraordinary conditions justify, to increase, from time to time for periods not exceeding thirty days, on the affirmative vote of five of its members, the amount of balances required by this Act to be maintained by member banks with their respective Federal reserve banks, provided such increase shall at no time exceed twenty per centum of such balances and shall be at the same rate for all member banks of any one district, and provided, further, that the Federal Reserve Board shall make a report to Congress in writing setting forth the conditions on which such action is based."

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COLLECTION OF CHECKS FOR NONMEMBER BANKS.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That the first paragraph of Section 13 of the Act approved December 23, 1913, as amended by the Act of September 7, 1916, be further amended so as to read 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 payable upon presentation, and also for collection, maturing bills, or, solely for purposes of exchange or of collection, may receive from other Federal reserve banks OR FROM NONMEMBER BANKS OR TRUST COMPANIES deposits of current funds in lawful money, national bank notes, or checks AND DRAFTS upon BANKS OR TRUST COMPANIES OR other Federal reserve banks ~~and checks and drafts~~ payable upon presentation within its district and maturing bills payable within its district; PROVIDED, HOWEVER, THAT NO FEDERAL RESERVE BANK SHALL RECEIVE CHECKS AND DRAFTS FROM A NONMEMBER BANK FOR THE PURPOSE OF EXCHANGE OR COLLECTION UNLESS SUCH NONMEMBER BANK MAINTAINS WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT A BALANCE IN AN AMOUNT TO BE DETERMINED BY THE FEDERAL RESERVE BOARD UNDER SUCH RULES AND REGULATIONS AS IT MAY PRESCRIBE.

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AMENDMENT TO SECTION 22.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATESOF AMERICA IN CONGRESS ASSEMBLED, That that part of Section 22 of the Act approved December 23, 1913, known as the Federal Reserve Act, which reads as follows:

> "Other than the usual salary or director's fees 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 business of the bank,"

be and hereby is amended and re-enacted so as to read as follows:

> "Other than the usual salary or director's ~~fees~~ FEE paid to any officer, director, ~~or~~ employee OR ATTORNEY of a member bank and other than a reasonable fee paid by said bank to such officer, director, ~~or~~ employee, OR ATTORNEY 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, PROVIDED, HOWEVER, THAT NOTHING IN THIS ACT CONTAINED SHALL BE CONSTRUED TO PROHIBIT A DIRECTOR, OFFICER, OR EMPLOYEE FROM RECEIVING THE SAME RATE OF INTEREST PAID TO OTHER DEPOSITORS FOR SIMILAR DEPOSITS MADE WITH SUCH BANK; OR TO PROHIBIT A DIRECTOR, WHO IS NOT AN OFFICER OR EMPLOYEE, FROM RECEIVING, DIRECTLY OR INDIRECTLY, THE USUAL AND CUSTOMARY COMMISSIONS OR FEES FOR SERVICES RENDERED IN BUYING AND SELLING SECURITIES OR OTHER INVESTMENTS FOR OR ON ACCOUNT OF SUCH BANK, BUT IN THIS LATTER CASE THE ACTION OF THE BOARD OF DIRECTORS, IN DIRECTING EACH PURCHASE OR SALE OF SUCH SECURITIES OR OTHER INVESTMENTS, MUST BE BY AN AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD EXCLUSIVE OF THE DIRECTOR INTERESTED, AND MUST BE RECORDED IN THE MINUTES OF THE MEETING OF SAID BOARD, SUCH MINUTES TO SPECIFY THE NAME OF THE DIRECTOR AND THE FIRM OR CORPORATION WITH WHICH HE IS CONNECTED, IF ANY, THROUGH WHICH SUCH ORDER IS TO BE EXECUTED TOGETHER WITH THE AMOUNT OF THE FEE OR COMMISSION TO BE PAID ON EACH TRANSACTION; AND, PROVIDED, FURTHER, THAT NOTES, DRAFTS, BILLS OF EXCHANGE OR OTHER EVIDENCES OF DEBT EXECUTED OR INDORSED BY DIRECTORS OF A MEMBER BANK MAY BE DISCOUNTED WITH SUCH MEMBER BANK ON THE SAME TERMS AND CONDITIONS AS OTHER NOTES, DRAFTS, BILLS OF EXCHANGE OR EVIDENCES OF DEBT UPON THE AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD OF DIRECTORS OF SUCH MEMBER BANK.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That the fifth paragraph of Section 13 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Acts approved March 15, 1915, and September 7, 1916, be and is hereby amended so as to read as follows:

> Any member bank may accept drafts or bills of exchange drawn upon it having not more than six months8 sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. No Member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, orcorporation to an ~~to~~ amount equal at any time in the aggregate to more than ten per centum of its paid-up and unimpaired capital stock and surplus unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance and no bank shall accept such bills to an amount equal at any time in the aggregate to more than one-half of its paid-up and unimpaired capital stock and surplus; ~~provided~~ PROVIDED, HOWEVER, THAT THE FEDERAL RESERVE BOARD, UNDER SUCH GENERAL REGULATIONS AS IT MAY PRESCRIBE, WHICH SHALL APPLY TO ALL BANKS ALIKE REGARDLESS OF THE AMOUNT OF CAPITAL STOCK AND SURPLUS, MAY AUTHORIZE ANY MEMBER BANK TO ACCEPT SUCH BILLS TO AN AMOUNT NOT EXCEEDING AT ANY TIME IN THE AGGREGATE ONE HUNDRED PER CENTUM OF ITS PAID-UP AND UNIMPAIRED CAPITAL STOCK AND SURPLUS, PROVIDED, HOWEVER, THAT THE AGGREGATE OF ACCEPTANCES GROWING OUT OF DOMESTIC TRANSACTIONS SHALL IN NO EVENT EXCEED FIFTY PER CENTUM OF SUCH CAPITAL STOCK AND SURPLUS.

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(Excerpt)

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 17 of the Act approved December 23, 1913, known as the Federal Reserve Act, be and is hereby amended so as to read as follows:

> Sec. 17. So much of the provisions of section fifty-one hundred and fifty-nine of the Revised Statutes of the United States, and section four of the Act of June twentieth, eighteen hundred and seventy-four, and section eight of the Act of July twelfth, eighteen hundred and eighty-two, and of any other provisions of existing statutes as require that before any national banking associations shall be authorized to commence banking business it shall transfer and deliver to the Treasurer of the United States a stated amount of United States registered bonds AND SO MUCH OF THOSE PROVISIONS OR OF ANY OTHER PROVISIONS OF EXISTING STATUTES AS REQUIRE ANY NATIONAL BANKING ASSOCIATIONS NOW OR HEREAFTER ORGANIZED TO MAINTAIN A MINIMUM DEPOSIT OF SUCH BONDS WITH THE TREASURER is hereby repealed.

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BRANCH BANKS

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 25 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act of September 7, 1916, be amended by adding a sub-section (a) to read as follows:

"Sec. 25a. That any member bank located in a city or incorporated town of more than one hundred thousand inhabitants and possessing a capital and surplus of $1,000,000 or more may, under such rules and regulations as the Federal Reserve Board may prescribe, establish branches, not to exceed ten in number, within the corporate limits of the city or town in which it is located; Provided, That no such branch shall be established in any State in which neither State banks nor trust companies may lawfully establish branches."

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MEMBERSHIP OF MUTUAL SAVINGS BANKS.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 9 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act of September 7, 1916, be amended by adding a subsection (a) to read as follows:

Section 9(a). Any mutual savings bank or association operating under the laws of any State, may make application to the Federal Reserve Board for the right to become an associate member of the Federal reserve bank of the district in which such savings bank or association is located.

The Federal Reserve Board under such rules and regulations as it may prescribe may permit such bank or association to become an associate member of the Federal reserve bank, but such Board before granting any application shall require satisfactory evidence that the laws of the State in which the applying bank or association is located, authorize such bank or association to engage in the business of a mutual savings bank and provide for a proper supervision over the operations of such bank or association.

Any mutual savings bank or association which becomes an associate member of a Federal reserve bank, shall agree to comply with all the provisions of Section 19 of this Act. Such associate members shall be entitled to all the clearing privileges granted to member banks, and Federal reserve banks shall be authorized to discount the promissory notes of such associate members having a maturity of not more than thirty days and which are se-

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cured, (a) by paper eligible for rediscount under Section 13 of the Federal Reserve Act, (b) by United States bonds, (c) by such municipal warrants as Federal reserve banks are authorized to purchase under the provisions of Section 14 of the Federal Reserve Act, or (d) by commercial paper or bankers' acceptances bearing the signature of not less than three persons, firms, or corporations.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That paragraph five of Section 18 of the Act approved December 23, 1913, known as the Federal Reserve Act, be and is hereby amended so as to read as follows:

> 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, OR ANY THREE PER CENT ONE YEAR GOLD NOTES ISSUED IN ACCORDANCE WITH THE PROVISIONS OF THIS SECTION, any Federal reserve bank making such deposit in the manner provided by existing law FOR THE DEPOSIT BY NATIONAL BANKS OF BONDS BEARING THE CIRCULATING PRIVILEGE, shall be entitled 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 NOTES OR bonds so deposited. Such CIRCULATING notes shall be obligations of the Federal reserve bank procuring the same, and shall be in form prescribed by the Secretary of the Treasury, and to the same tenor and effect as national bank notes now provided by law. They shall be issued and redeemed under the same terms and conditions as national bank notes except that they shall not be limited to the amount of the capital stock of the Federal reserve bank issuing them. CIRCULATING NOTES OF FEDERAL RESERVE BANKS SECURED BY THREE PER CENT ONE YEAR GOLD NOTES SHALL BE SUBJECT TO THE SAME TAX IMPOSED BY LAW ON CIRCULATING NOTES WHICH ARE SECURED BY THREE PER CENT BONDS OF THE UNITED STATES.

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AN AMENDMENT TO SECTION 4 OF THE FEDERAL RESERVE ACT.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 4 of the Act approved December 23, 1913, known as the Federal Reserve Act, be amended by striking out the sentence reading as follows: "One of the directors of Class C, who shall be a person of tested banking experience, shall be appointed by the Federal Reserve Board as deputy chairman and deputy Federal reserve agent to exercise the powers of the chairman of the board and Federal reserve agent in case of absence or disability of his principal", and by adding in place thereof the following:

"Subject to the approval of the Federal Reserve Board, the Federal reserve agent shall appoint one or more assistants. Such assistants, who shall be persons of tested banking experience, shall assist the Federal reserve agent in the performance of his duties and shall also have power to act in his name and stead during this absence or disability. The Federal reserve agent may require such bonds of his assistants as he may deem necessary for his own protection. Assistants to the Federal reserve agent shall receive an annual compensation to be fixed and paid in the same manner as that of the Federal reserve agent."

1/3/16.

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OATH OF

FEDERAL RESERVE AGENT OR DEPUTY FEDERAL RESERVE AGENT.

(Other Class "C" directors may use this form, with references to Federal reserve agent eliminated).

State of _____ :
: ss
City or County of _____ :

I, the undersigned, having been appointed a Class "C" director of the Federal Reserve Bank of _____, located in the Federal Reserve City of _____, State of _____, and in District No. _____, as determined in accordance with the provisions of the Federal Reserve Act, and having been designated as (Deputy) Federal Reserve Agent by the Federal Reserve Board, being a citizen of the United States and resident of the State of _____, do solemnly swear (affirm) that I will, so far as the duty devolves upon me, diligently and honestly administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks; that I will not knowingly violate, or willingly permit to be violated any of the provisions of the Statutes of the United States under which this bank has been organized; that I will well and faithfully discharge the duties of the office of (Deputy) Federal Reserve Agent on which I am about to enter; that I am not an officer, director, employee, or stockholder in any other bank; and that I take this obligation freely without any mental reservation or purpose of evasion.

Subscribed and sworn (affirmed) to before the undersigned, a Notary Public in and for the State and _____ aforesaid, this _____day of _____, 191 .

_____
Notary Public.

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947a.

COLLECTION OF CHECKS FOR NONMEMBER BANKS.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That the first paragraph of Section 13 of the Act approved December 23, 1913, as amended by the Act of September 7, 1916, be further amended so as to read 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 payable upon presentation, and also for collection, maturing NOTES AND bills; or, solely for purposes of exchange or of [redacted]collection, may receive from other Federal reserve banks deposits of current funds in lawful money, national bank notes, or checks upon other Federal reserve banks and checks and drafts payable upon presentation within its district and maturing NOTES AND bills payable within its district; OR, SOLELY FOR THE PURPOSES OF EXCHANGE OR OF COLLECTION, MAY RECEIVE FROM ANY NONMEMBER BANK OR TRUST COMPANY DEPOSITS OF CURRENT FUNDS IN LAWFUL MONEY, NATIONAL BANK NOTES, FEDERAL RESERVE NOTES, CHECKS AND DRAFTS PAYABLE UPON PRESENTATION OR MATURING NOTES AND BILLS, PROVIDED SUCH NONMEMBER BANK OR TRUST COMPANY MAINTAINS WITH THE FEDERAL RESERVE BANK OF ITS DISTRICT A BALANCE IN AN AMOUNT TO BE DETERMINED BY THE FEDERAL RESERVE BOARD UNDER SUCH RULES AND REGULATIONS AS IT MAY PRESCRIBE.

1/6/17.

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page 1815 out of order - See just before 1814

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
948 FEDERAL RESERVE BOARD

January 2, 1917.

Dear Sir:

Under separate cover we are forwarding 150 copies of Revised Form 38 for reporting distribution by maturities and classes of bills and short-term investments on hand at close of business on Fridays.

Your special attention is called to the lower portion of the form, requesting information as to the various classes of discounted paper on hand under the two-fold head of secured and unsecured bills.

Please discontinue use of old Form 38 and report the information requested on the new form, beginning with January 5 of the present year.

Respectfully,

Secretary.

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AN AMENDMENT TO SECTION 4 OF THE FEDERAL RESERVE ACT.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 4 of the Act approved December 23, 1913, known as the Federal Reserve Act, be amended by striking out the sentence reading as follows: "One of the directors of Class C, who shall be a person of tested banking experience, shall be appointed by the Federal Reserve Board as deputy chairman and deputy Federal reserve agent to exercise the powers of the chairman of the board and Federal reserve agent in case of absence or disability of his principal", and by adding in place thereof the following:

"Subject to the approval of the Federal Reserve Board, the Federal reserve agent shall appoint one or more assistants. Such assistants, who shall be persons of tested banking experience, shall assist the Federal reserve agent in the performance of his duties and shall also have power to act in his name and stead during this absence or disability. The Federal reserve agent may require such bonds of his assistants as he may deem necessary for his own protection. Assistants to the Federal reserve agent shall receive an annual compensation to be fixed and paid in the same manner as that of the Federal reserve agent."

1/3/16.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That paragraph five of Section 18 of the Act approved December 23, 1913, known as the Federal Reserve Act, be and is hereby amended so as to read as follows:

> 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, OR ANY THREE PER CENT ONE YEAR GOLD NOTES ISSUED IN ACCORDANCE WITH THE PROVISIONS OF THIS SECTION, any Federal reserve bank making such deposit in the manner provided by existing law FOR THE DEPOSIT BY NATIONAL BANKS OF BONDS BEARING THE CIRCULATING PRIVILEGE, shall be entitled 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 NOTES OR bonds so deposited. Such CIRCULATING notes shall be obligations of the Federal reserve bank procuring the same, and shall be in form prescribed by the Secretary of the Treasury, and to the same tenor and effect as national bank notes now provided by law. They shall be issued and redeemed under the same terms and conditions as national bank notes except that they shall not be limited to the amount of the capital stock of the Federal reserve bank issuing them. CIRCULATING NOTES OF FEDERAL RESERVE BANKS SECURED BY THREE PER CENT ONE YEAR GOLD NOTES SHALL BE SUBJECT TO THE SAME TAX IMPOSED BY LAW ON CIRCULATING NOTES WHICH ARE SECURED BY THREE PER CENT BONDS OF THE UNITED STATES.

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MEMBERSHIP OF MUTUAL SAVINGS BANKS.

BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 9 of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act of September 7, 1916, be amended by adding a subsection (a) to read as follows:

Section 9(a). Any mutual savings bank or association operating under the laws of any State, may make application to the Federal Reserve Board for the right to become an associate member of the Federal reserve bank of the district in which such savings bank or association is located.

The Federal Reserve Board under such rules and regulations as it may prescribe may permit such bank or association to become an associate member of the Federal reserve bank, but such Board before granting any application shall require satisfactory evidence that the laws of the State in which the applying bank or association is located, authorize such bank or association to engage in the business of a mutual savings bank and provide for a proper supervision over the operations of such bank or association.

Any mutual savings bank or association which becomes an associate member of a Federal reserve bank, shall agree to comply with all the provisions of Section 19 of this Act. Such associate members shall be entitled to all the clearing privileges granted to member banks, and Federal reserve banks shall be authorized to discount the promissory notes of such associate members having a maturity of not more than thirty days and which are se-

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cured, (a) by paper eligible for rediscount under Section 13 of the Federal Reserve Act, (b) by United States bonds, (c) by such municipal warrants as Federal reserve banks are authorized to purchase under the provisions of Section 14 of the Federal Reserve Act, or (d) by commercial paper or bankers' acceptances bearing the signature of not less than three persons, firms, or corporations.

1/3/17

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CHAIRMAN
JOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

952

WASHINGTON

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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

January 4, 1917.

Dear Sir:

I am sending you herewith four copies of drafts of the various amendments which have been prepared by the Board and submitted after discussion to the Committees on Banking and Currency of the Senate and the House of Representatives. You will see the amendments cover the following subjects:

1. AMENDMENT TO SECTION 16 which provides

   (a) for the issue of Federal reserve notes directly against the deposit of 100% gold; or 100% of paper, or both.

   (b) for the counting of gold held by the Federal reserve agents as security for notes, as part of the gold reserve required to be held by the bank against such Federal reserve notes.

This amendment was approved and endorsed by a majority of the Board.

2. AMENDMENT OF SECTION 19 abbreviating and simplifying the clauses in Section 19 which relate to reserve requirements. This

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proposed amendment provides that all member banks shall maintain reserves in the Federal Reserve Bank as follows:

	Against Demand Deposits	Against Time Deposits
(a) Country Banks	7%	3%
(b) Reserve City Banks	10%	3%
(c) Central Reserve City Banks	13%	3%

and in addition every member bank is required to keep in its own vault for till money an amount of specie or currency (not necessarily gold or lawful money) equal to five per cent of its demand deposits, less the amount of net balances with Federal Reserve Banks in excess of the minimum above stipulated.

3. 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.

4. AMENDMENT OF SECTION 16 to permit nonmenber 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.

5. AMENDMENT OF SECTION 22 - the penal statute - so as to define more clearly the rights and limitations of directors in the matter of

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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 services is not incumbent upon them in their capacity as directors.

6. 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.

7. 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.

8. 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.

9. 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.

10. AMDNEMENT OF SECTION 18 so as to give to United States one year 3% gold notes in the hands of Federal reserve banks the

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circulation privilege for the issuance of Federal reserve bank notes.

11. 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.

Very truly yours,

Governor.

Inclosure.

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STATEMENT FOR THE PRESS.

January 9, 1917.

The Boston Clearing House banks have adopted a new form designed to show the change in their reserve position from week to week, as given at the bottom of their usual clearing house bank statement. In the past they have announced the deficiency or excess of their vault cash, and also their deficiency or excess with the Federal reserve bank.

Since the adoption of the ruling making it optional with member banks to keep reserves in vault or in the Federal reserve bank, the Boston banks have shown a deficiency in their vault cash, and an excess with the Federal reserve bank. It has been felt that these items might properly be consolidated just as similar figures are conbined in English bank statements, and that such consolidation would be a final recognition on the part of the Clearing House that deposits with the Federal reserve bank are practically interchangeable (so far as reserve availability is concerned) with cash in vault. When the matter was recently called to the attention of the Clearing House Committee in Boston, the members acquiesced in the suggested change. This is regarded as a further indication of the desire of the larger New England banks to cooperate with the Federal reserve bank in every way possible.

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

960.

January 8, 1917.

Dear Sir:

The Federal Reserve Board has to-day determined, in the exercise of the discretion vested in it under the provisions of Section 18 of the Federal Reserve Act, that it will not require Federal Reserve Banks to purchase during the year 1917 more than fifteen million dollars of United States bonds offered for sale by member banks through the Treasurer of the United States. It will require Federal Reserve Banks to purchase on April 1, 1917, the full amount of this fifteen million dollars, or so much thereof as may be offered for sale on or before March 21st.

Under the provisions of Section 18 Federal Reserve Banks are not permitted to purchase from member banks through the Treasurer more than twenty-five million dollars of bonds in any one year, less the amount of bonds bearing the circulation privilege acquired in the open market during that year. If, therefore, Federal Reserve Banks are desirous of giving member banks an opportunity to sell the full amount of fifteen million dollars under the provisions of Section 18, they should refrain from investing in the open market during the first quarter anything in excess of the difference between fifteen million dollars and twenty-five million dollars.

Please bring this to the attention of your executive committee.

Respectfully,

Governor.

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STATEMENT FOR THE PRESS.

January 9, 1917.

The Federal Reserve Board has determined, in the exercise of the discretion vested in it under the provisions of Section 18 of the Federal Reserve Act, that it will not require Federal reserve banks to purchase during the year 1917 more than $15,000,000. of United States bonds offered for sale by member banks through the Treasurer of the United States. It will require Federal reserve banks to purchase on April 1, 1917, the full amount of this $15,000,000. or so much thereof as may be offered for sale on or before March 21st, the last day on which applications will be received by the Treasurer for the sale of bonds on April 1st.

Under the provisions of Section 18 Federal reserve banks are not permitted to purchase from member banks through the Treasurer more than twenty-five million dollars of bonds in any one year, less the amount of bonds bearing the circulation privilege acquired in the open market during that year. There is no limit imposed by law on the amount of bonds which may be purchased in the open market by Federal reserve banks.

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ANNUAL REPORT

TO THE SPEAKER OF THE HOUSE OF REPRESENTATIVES:

SIR:

The Federal Reserve Board transmits herewith its annual report for the calendar year 1916.

This report, the third submitted, is made just after the close of a year of unexampled commercial, industrial and financial activity in the United States. Never before in time of domestic peace have wages and prices reached such high levels. In practically all important industries labor and capital have throughout the year found full and remunerative employment. The situation may best be summed up in the statement that during the calendar year 1916 exports of merchandise from the United States to other countries amounted to about $5,460,000,000, while its imports amounted to about $2,360,000,000, leaving a net trade balance in favor of the United States of about $3,100,000,000. Domestic trade, stimulated as it has been by the presence of

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unusually high wages and prices, has developed an activity paralleling that of the nation's foreign business, and the results of this whole situation have been reflected in the augmentation of bank resources, as illustrated by the fact that the deposits of all banks and trust companies in the United States have shown an increase during the year of not less than $4,300,000,000.

INFLOW OF GOLD AND ATTENDANT PROBLEMS.

Since the beginning of the European war the problem incident to the distribution of gold throughout the world, as far as the United States is concerned, has been reversed. It will be remembered that at the outbreak of the war American importers and banking houses were indebted to their correspondents abroad on current account to the extent of about $450,000,000. The liquidation of this indebtedness at first involved not only large shipments of gold, but the conditions under which gold could be exported were such as to add greatly to the normal cost of settlements.

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To assist in this situation there was organized, at the instance of the Federal Reserve Board, a bankers' gold fund of $100,000,000, the operations of which were fully reviewed in the first annual report made by this Board. Due to the availability of the facilities provided by this gold fund, as well as to the increasing volume of our exports to Europe, balances shortly began to appear in favor of this country. These balances have increased ever since at an unprecedented rate. The Board has information showing that from the beginning of the war until the end of December 1916, there was a net movement of gold into the United States of approximately $870,000,000, and it is estimated that during the same period no less than $2,500,000,000 of securities of American origin, including obligations of the national Government, of States, of municipalities, and of firms, corporations and individuals, have been transferred from foreign to domestic ownership. During this period, according to trustworthy estimates, about $2,000,000,000 of securities issued by foreign Governments,

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corporations and firms, have been absorbed and are now held by American financial institutions and investors. European holdings of American securities have thus been correspondingly reduced, and for the near future, at least, the United States must choose between the extremes of excessive importations of gold on the one hand, and the undue absorption of the credit obligations of foreign countries on the other, or it must adhere to a safe middle course. In these circumstances, the manifest duty of the Federal reserve banks has been to encourage conservatism, and so far as possible to prevent undue and unwise extensions of credit. The year's business did not develop even the seasonal demand which on some occasions requires action and which, during the year 1915 led the Board to establish what is known as the commodity rate, designed particularly to aid producers during the crop-moving season. To a great degree the ease of money and smoothness of operation of our financial machinery have been due

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to the facilities afforded and to the confidence inspired by the Federal reserve system; as well as to the largely increased stock of reserve money resulting from the importations of gold. During the year there was a comparatively light demand on the part of member banks for rediscount accommodations, the maximum amount of rediscounted paper held by the Federal reserve banks being $38,345,000 on December 8; and the activities of the Federal reserve banks have been chiefly under the open market provision of the law in the purchase of acceptances, of Government bonds, and of municipal warrants. Transactions of these kinds were engaged in to such an extent that the total invested resources of all Federal reserve banks on December 30, 1916, amounted to $221,897,000. As already indicated, the Board's principal problem has been that of maintaining, so far as possible, the liquid condition of the banking community, and in this it was of course primarily concerned with the business of the Federal reserve banks themselves. The Federal Reserve Act prohibits the investment of funds

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of Federal reserve banks in long-term securities, excepting only bonds and notes of the Government of the United States; and, keeping in mind the spirit, as well as the letter of the Act, the Board has recently in two instances deemed it necessary to take decisive action. The first was in connection with the use of bankers' acceptances in international transactions. The American acceptance is now well established in the world's markets, being known in almost all parts of the globe, and even in those countries which three years ago had a monopoly of the acceptance business, American credit facilities are now being freely used. The development of this acceptance business has been highly gratifying and the Federal reserve banks have done their full part in promoting its growth, as they have been liberal purchasers of acceptances. More than a year ago, in August 1915, the Board was informed of certain renewals of acceptance credits which clearly grew out of the shipment of goods in the first instance, and it

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ruled that, as a matter of principle, such acceptances need not be excluded and that Federal reserve banks might consider as eligible bills having not longer than three months to run, drawn under such credit arrangements. It was found, however, during the latter part of 1916, that renewal acceptances were being offered on the market in increasing volume, and the Board took occasion to warn Federal reserve banks, and through them the member banks, against unduly large purchases of paper which, while eligible in form, might not be in fact or in essence of a true self-liquidating character. It is, of course, proper to extend acceptance credits in liberal amounts to facilitate commercial transactions all over the world, and the Board expects to see business of this kind grow into very large figures, but it feels that banks should not permit mere considerations of profit to cause them to disregard long established and sound principles, the observance of which is so necessary for safety. One fundamental rule governing the bankers' acceptance is that the acceptance should finance

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the drawer and not the accepting bank. When a banker makes a cash advance at a given rate of interest for a certain length of time, his debtor should not draw upon him for the purpose of enabling the banker to reimburse himself by the sale of his acceptance for the advance which he has made to the borrower. This process would make it possible for a long-term borrowing to be financed by an accommodation bill drawn for the benefit of the banker; and such a draft would not be essentially self-liquidating. The real borrower may have secured the advance by renewal agreements for a long-term at a fixed rate for the entire time and not subject to readjustment at any renewal period. In such a case the borrower is not concerned with the discount transaction, and when the first bill matures the advance will continue to run and no increase in rate would cause the borrower to cover his acceptance and seek accommodation elsewhere, because during the term of the extended credit he would have no interest in the

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discount rate of the country upon which he has drawn. The acceptor and not the actual debtor would be the borrower in the discount market, and as regards the original borrower the acceptance would become merely an accommodation draft for the benefit of the acceptor, who alone would be subject to the changing vicissitudes of the discount market. It is clear in the second place, that drafts drawn in one country upon another against long-term securities are not self-liquidating, no matter how short the time the drafts themselves may have to run. Where acceptances are based upon actual commercial transactions the sum total of the acceptance bears a definite relation to, and is regulated by the volume of international trade, but when bills are accepted against securities, this automatic regulation disappears, and if finance bills are permitted to be drawn without discrimination they would continue to accumulate just as long as there is a substantial difference

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in the interest rates of the two countries concerned. It is entirely natural and proper that countries or sections where wealth has accumulated and which have large holdings of gold ... should afford credit facilities to others not so fortunately situated in this respect. As between nations this can be done through short commercial credits by means of bankers' acceptances, where the acceptance is liquidated out of funds coming from the borrower before maturity; or strictly as an investment proposition, by transactions outright in securities issued or held by citizens of the borrowing country. Both methods may be perfectly sound, but dealers in credit should distinguish clearly between the two transactions. We must be careful not to confuse commercial banking with investment banking, nor should we permit our discount market to become so saturated with offerings intrinsically of an investment character as to influence discount rates and impede the free operation of the discount market, which is intended to deal in short-term or commercial borrowings and should not be used or abused to serve merely as an adjunct of the investment market.

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The second occasion which in the Board's judgment called for action arose out of the trend toward absorption of foreign securities by the banks of this country, and because of the announcement that Treasury bills, nominally short term, but obviously repayable, if placed in large volume by the sale of additional securities of the same kind were about to be offered on the market in an indeterminate amount. The Board felt that such purchases in any considerable volume would in existing circumstances tend to place the onus upon the Federal Reserve Banks because while bills of this character are admittedly ineligible for rediscount or purchase by Federal reserve banks, the member banks would rediscount with the Reserve institutions eligible paper in order to replenish their reserves which might have been depleted through purchases of such Treasury bills. The Board accordingly, on November 28, made a public statement in which the banks were cautioned against investing too freely in the proposed offerings. This action was taken not because of any doubt as to the ultimate payment of the obligations, but merely because they obviously did not constitute a liquid banking investment. The Board stated that, in its opinion, member banks should

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pursue a policy of keeping themselves liquid; of not loaning down to the legal limit, but of maintaining an excess of reserves - not with reserve agents, where their balances are loaned out and constitute no actual reserve, but in their own vaults or preferably with their Federal Reserve banks. The Board advised banks that they should proceed with much caution in locking up their funds in long term obligations or investments which are short term in form or name but which may in the aggregate have to be renewed until normal conditions return. The Board does not feel that it is incumbent upon it to advise private investors and so stated, but in view of the fact that the United States is becoming the banker of foreign countries throughout the world, and as securities of various kinds are being offered in our markets, the Board took occasion to suggest that particularly in the case of unsecured loans, investors should receive full and authoritative data. In making this statement, it was not the purpose of the Board to question the credit of any government, nor did it seek to reflect upon any particular obligations. The Board sought merely to indicate that the same business like habits which

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are well established regarding domestic loans should be developed in the marketing of foreign flotations. It is the practice of every issuing house in offering securities to furnish specific information and to give all necessary details either over its own signature or that of the head of the borrowing corporation. The importance of complete and authentic information is nowhere more fully understood and appreciated than in Europe; and in foreign countries a prospectus contains all the important facts relating to the loan, in a statement signed by an authorized representative of the government or by the issuing house, or in some cases by both. The timeliness of the Board's statement was demonstrated by the fact that, notwithstanding the fact that this offering of foreign bills was withdrawn shortly after the statement appeared, there was a notable stiffening of rates for call loans in our principal money market, which advanced to 15%, a higher level than they had reached since the establishment of the Federal reserve banks. It developed that the reserves of the banks in our most important money center were, as a matter of fact, none too large, and that the money tension, which was felt how-

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ever, only in the case of collateral loans not eligible for rediscount at the Federal reserve banks, was eased by the resumption of gold imports on a large scale.

CONSERVATION OF GOLD SUPPLY

The Board, however, has recognized from the first that merely negative or preventive measures such as those just referred to can not be expected to meet all the requirements of the unusual situation with which the country has been confronted and it has realized that decisive steps enlarging the power of the Federal reserve banks to conserve and protect the country's gold supply ought to be taken. In the statement of November 28th above referred to, the Board announced that it would ask Congress to advance the date upon which the final transfer of reserves from correspondent banks in reserve and central reserve cities to the Federal reserve banks would take place, and suggested that this date, originally fixed on November 16, 1917, be advanced to February or March. There are several reasons for urging this consideration upon

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the immediate attention of Congress. The United States has today a plethora of gold, and while the Board does not believe that further importations of the metal must of necessity prove a source of danger or disturbance, it is desirable, in order to avoid danger, to control the inflowing gold and not permit it to become the basis of abnormal loan expansions and of inflation. The abstract of reports made by all national banks on November 7, 1916, shows a surplus of about $1,016,000,000. This surplus is based upon the reduced reserves permitted under the Federal Reserve Act, and its enormous size is due in part to the further fact that interior banks are still able to count balances with national bank agents as reserve. The law now provides that after November 16th the entire reserves of member banks must be carried partly in their own vaults and partly with the Federal reserve bank of their district. It is estimated that the reserves of country banks carried with reserve city correspondents represent about $150,000,000, and the effect of a possible withdrawal of this sum from the reserve depositories next November has been viewed with some apprehension; but with the larg

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surplus reserve now carried by the banks, it does not seem that there would be any withdrawals necessary should the date for the final transfer be advanced as suggested by the Board. The present reserve required against existing deposit liability of national banks is $1,456,000,000. Banks hold $2,472,000,000, of reserves, of which $1,437,000,000 consists of cash in vault and balances with Federal reserve banks, where all reserves must ultimately be concentrated. From this it appears that only $19,000,000 must be taken out of the balance of $1,035,000,000 now carried by the banks with national bank reserve agents in order to give the banks the entire reserve required. This process would give the banks their exact reserve requirements in vault and with Federal reserve banks and would leave no surplus reserve at all. This would not necessarily alter the technical position of the banks in the slightest degree, for the city banks would have balances with their country correspondents just as before, with the exception of the comparatively small amount required to be transferred, and the only difference would be that balances with former reserve correspondents would no longer count as bank reserves, but in addition

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other respects would provide for the same functions as at present.

The Board has given much attention to the whole reserve problem and has transmitted to the Chairmen of the appropriate committees recommendations for further amendments to the Federal Reserve Act, which had been agreed upon by a majority of the Board. The text of these suggested amendments is presented in exhibit _____, but as two of them are directly connected with the control and conservation of our gold supply, it is deemed proper to make particular reference to them at this point. The two amendments are as follows:

(Insert note issue amendment and amendment regarding reserves.)

When the Federal Reserve Act was drafted its principal object was to deal with national problems of banking and currency, but 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

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somewhat in order to enable us to deal effectively with the international problems which now confront us and 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, and the other the excessive and unregulated outflow of gold. The amendments proposed by the Board 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 whatever the developments may be leading to the flow of gold back into Europe, or to South America or to the Orient, the gold may be released by the banks of this country without forcing any violent contraction of loans or causing undue disturbance to legitimate business. At present out of approximately two and three-quarter billions of gold in this country there are held or controlled by Federal reserve banks about $738,000,000 . Of this amount $283,000,000 is held by Federal Reserve Agents as security for Federal reserve notes outstanding

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and $455,000,000 are reserve money and must therefore be used conservatively. But even if we assume that the Federal reserve banks would be willing to reduce their gold reserves to 40% of their deposits and note liability (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 $300,000,000. While this is a very large sum its sufficiency may well be questioned 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 in circulation at present from seven to eight hundred million dollars in gold and gold certificates, and that there are at present held in the vaults of member banks about $768,000,000 of reserve money. There should be added to this estimate about $600,000,000 of lawful money in the vaults of nonmember State banks and trust companies. It is difficult to estimate the amount of gold that is hoarded by individuals or carried as pocket money. The amount is no doubt substantial, but whatever it may be, it

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is lost for reserve purposes and is not fulfilling its true and highest function. The use of gold as a medium of domestic circulation is a natural waste. The tendency in foreign countries in normal times has been to substitute Government bank circulation for the use of metallic gold and to concentrate the gold itself in the central banks. 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 one form or another of United States currency. To the extent of about three hundred million dollars Federal reserve note circulation has been substituted for gold certificates. Under the requirements of the present law, however, 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 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 system is unable to show the greater strength which might be

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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. The control of gold by Federal reserve banks in times of plethora 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, and will enable us more safely and effectively to proceed with the development of our foreign trade and to give the necessary credit facilities for building it up. We should be in a position to face conditions which may call for an outflow of gold without any jar to 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

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actual circulation while enabling them at the same time to release gold which at present is tied up in their own vaults. The amendments are proposed on 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 centering it, as far as possible, in the hands of the Federal reserve banks, where it can be protected effectively when not required and used effectively in times of need. The member bank does not require gold so much as currency with which to supply the ordinary demands of its depositors. 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 September 12, 1916 the gold holdings of all member banks were about $500,000,000. Under the proposed amendment of Section 19 $350,000,000 of this amount would be transferred to the Federal reserve banks. Proceeding upon this theory, the Board believes that ulti-

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mately the law should require of member banks no more than that they should maintain a certain balance with the Federal reserve banks, and that the Federal reserve banks must have sufficient reserves of gold with which to protect the country's gold obligations, but that there should be no legal requirement as to the reserves that a member bank should carry in its own vault, which 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 too extreme, particularly under present conditions, and nothing should be done that might tend to a further release of reserve money. It was thought advisable, therefore, to prescribe a minimum amount of currency that the member banks should be required to keep in their vaults. The amount suggested is 5% of the demand deposits, so that the present reserve requirements will remain practically unchanged. While the effect of some of the changes as proposed, will be to reduce somewhat the reserve requirements, the reserves will be increased by the abrogation of the privilege that the

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member banks have hitherto had 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, but the important result will be 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. On November 16, 1916, the final installment of member banks' obligatory reserve, amounting to $60,000,000, was paid into the Federal reserve banks by their members, Under the provisions of the Federal Reserve Act about $260,000,000 of reserves were paid in to the Federal reserve banks immediately upon their organization. The Act provides that subsequent reserve payments should be made at intervals of six months, and accordingly on May 16,

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1915, November 16, 1915, May 16, 1916 and November 16, 1916, additional percentages of reserves were transferred. Due partly to these regular transfers of reserves as required by the law on the dates specified, and partly to the change in vault reserve requirements provided by the mandatory Act of September 7, 1916, the money stock of Federal reserve banks has been greatly strengthened, the actual holdings on successive dates being as follows:

December 31, 1914	$255,647,000
June 30, 1915	300,814,000
December 31, 1915	357,983,000
June 30, 1916	404,206,000
December 31, 1916	540,000,000

No further payments are now compulsory, but from and after November 16, 1917, (or earlier if the Board's suggested amendment should be adopted) balances with reserve agents in reserve and central reserve cities will no longer count as member banks' reserves, and members will be required to build up either their vault cash or their balances with Federal reserve banks sufficiently to cover the required reserves heretofore carried as balances with correspondents.

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DEVELOPMENT OF DISOUNT RATES.

Except for a slight stiffening of rates of discount toward the close of the year resulting in an increase of rates in some districts by one-half of one per cent, the rates prevailing at Federal reserve banks have been nearly stationary throughout the year. Of the changes made, the only one likely to be of much importance, was in the rate on acceptances, which was first advanced by the Federal Reserve Bank of New York in consequence of a firmer tendency in the money market. The idea of establishing a differential rate for acceptances, designed to favor those made by member banks of the Federal reserve system, has also been adopted by some of the Federal reserve banks, and is a desirable innovation.

There has been no occasion to establish new or special rates designed for the accommodation of particular industries or sections. The plan of applying a low "commodity rate", established by the Board in September 1915, for the benefit of producers and shippers of agricultural products, has continued operative,

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although the rate itself was raised to 3-1/2 and 4% at some of the banks, but the need for its application has been less than it was a year ago. The high prices of all agricultural products, and the general and sustained demand for them, not only at home but throughout the world, has brought to the farmers of the country a degree of prosperity and a supply of fluid resources wholly unprecedented. This has, in no small degree, delieved them of dependence upon banks for current accommodation, while it has also led them to place their products upon the market without holding them in order to obtain better prices than could be had at the close of the growing season. Not only the farmer, but practically every other element in the commercial community has been strong and self-dependent, due to the high return on labor and capital, and the prevailing ease in the money market. The influence of the Federal reserve banks upon rates has, therefore, continued throughout the present year, as in the past, to be potential and indirect, and has not been felt either as the result of large operations, or

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of positive action designed to relieve banks or borrowers.

A comparison of discount rates prevailing at Federal reserve banks shows that the principal difference between conditions the past year and the previous one lies in the somewhat greater diversification of rates, the new 15-day rate having been introduced for the greater convenience of member banks desiring temporary accommodations. Perhaps there is no better commentary upon some of the factors that have led to the transfer of discount business to the United States, than a comparison of rates prevailing in the principal foreign markets with those in New York. A notable difference is shown by the following figures contrasting the range of bank rates in the principal financial markets:

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	Bank rates in 1916.
London	5 - 6
Paris	5
Berlin	5
Rome	5
Petrograd	6
Amsterdam	4-1/2
Stockholm	4-1/2 - 5-1/2
Christiania	4-1/2 - 5
Copenhagen	5
Madrid	4-1/2
New York	2 - 2-3/4

DEVELOPMENT OF FEDERAL RESERVE CIRCULATION.

Reference has already been made to the maintenance and increase of the actual gold stock of the nation as represented by the reserves of the Federal reserve banks, as a fundamentally necessary factor in the solution of existing financial problems; and the plans and policy of the Federal Reserve Board for the pro-

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tection and enlargement of this gold stock, have been outlined. It should further be explained at this point that the Federal reserve note has played an important part in potentially assisting the enlargement of the gold stock at Federal reserve banks, and at the same time in checking an inflationary process that might otherwise have arisen. The rapid inflow of gold into the United States, if not diverted largely to Federal reserve banks, as it could not wholly be under any conditions, naturally tends to promote an inflationary tendency in prices, and an over-extension of banking credit, an admitted element of danger. Even if the new accumulation of gold could be successfully directed to the vaults of the reserve banks, there would still exist some tendency toward inflation as the result of greatly augmented resources. But as a matter of fact as the new gold has come into circulation a considerable portion of it has been brought to at least one of the reserve banks for the purpose of exchange for Federal reserve notes.

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The Federal reserve agents' holdings of gold from January 1, 1915, to December 30, 1916, increased $270,270,000, while our net imports of gold for that period were $953,130,000. The Federal Reserve Act nowhere makes provision for any such direct exchange of notes for gold, but some of the Federal reserve banks, with the Board's sanction, have adopted the expedient of obtaining notes from the Federal reserve agent against a deposit of eligible paper, following this operation by a deposit of gold and withdrawal of the collateral, and then again depositing the collateral and obtaining notes. It is evident that in this way Federal reserve notes could be obtained upon practically the same basis as if they had been directly issued against a deposit of gold coin; and by repeating the transfer of collateral a sufficient number of times, any amount of reserve notes within the limit of the gold reserve required, could be placed in circulation. Largely as the result of this operation there has been issued, and was outstanding on December 30, a

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total sum of $310,110,000 of Federal reserve notes. The true character of these notes is evident when it is seen that the security protecting them is sligible commercial paper only to the extent of $18,593,000, while $282,522,000 of it consists of actual gold. The issue of notes thus far put out has, in fact, been primarily effected as a direct exchange of notes for gold.

CONVERSION OF BONDS

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RETIREMENT OF NATIONAL BANK NOTES.

Under Section 16 of the Federal Reserve Act, Federal reserve banks may be required to purchase $25,000,000 of United States bonds, and a ruling of the Secretary of the Treasury under that Section permits them to convert through the Treasury Department $30,000,000 into thirty-year 3% United States bonds and one-year 3% Treasury notes.

United States bonds actually purchased by Federal reserve banks during 1916 exceeded $25,000,000, the amount which Federal re-

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serve banks may be required to purchase during any one year, and at no quarterly period was it necessary for the Federal Reserve Board to direct the purchase of bonds under Section 18 of the Federal Reserve Act.

The full amount of $30,000,000 in conversion bonds and one-year notes was taken by the 12 Federal reserve banks, an allotment based upon capital being made to each. Three banks, those at Boston, Philadelphia and San Francisco, did not avail themselves of the full conversion privilege; and the difference between the full quota of these banks and the amounts applied for by them, $1,918,900, was distributed among seven other banks which had applied to convert more than their allotment. Conversion bonds amounting to $15,761,000, and one-year notes amounting to $14,239,000, were issued for the year ending September 30, 1916. For the quarter ending December 31, 1916, Federal reserve banks converted $18,597,200, of which $9,301,000 was notes, and $9,306,600 bonds, the Board hav-

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ing previously announced that it would approve the applications of Federal reserve banks for the conversion of all or any portion of their full annual allotment on January 1, 1917, or the beginning of any other quarterly period.

Inasmuch as the banks had thus already purchased bonds to an amount equalling more than half their quotas, they were advised, in an announcement made on January 8, 1917, that the Board would not require them to purchase during the year 1917 more than $15,000,000 of United States bonds offered for sale by member banks through the Treasury of the United States, and that it would require Federal reserve banks to purchase on April 1, 1917, the full amount of this $15,000,000, or so much thereof as might be offered for sale by member banks prior to March 21.

The original purpose of the bond conversion of the Federal Reserve Act was two-fold - that of protecting the value of United States bonds deposited to secure circulation, and that of insuring a gradual but steady retirement of national bank notes, the gap

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thus left, to be filled, so far as necessary, by Federal reserve currency. During the past year national banks have withdrawn from deposit with the Treasurer of the United States bonds deposited to secure circulation of the par value of $_____. They have deposited lawful money to retire outstanding notes in the sum of $_____. The total of national bank notes outstanding at the beginning of the year 1916 was $_____, while on December 30, 1916, the amount outstanding was $_____, a reduction of $_____.

Federal reserve banks sold in 1916 new bonds and conversion notes as follows:

Section 16 of the Federal Reserve Act permits Federal reserve banks to issue bond-secured currency known as Federal reserve bank notes, protecting them by deposited bonds, as in the case of national bank notes. Under this provision of the law the total amount of Federal reserve bank notes issued to December 31, 1916, was $12,054,980. There were held at the close of 1916 by the Fed-

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eral Reserve Bank of Kansas City, $6,000,000, and by the Federal Reserve Bank of Dallas $2,000,000. The remaining amount is in circulation or in the Treasury of the United States. Federal reserve banks have extinguished their liability on account of $4,000,000 of these notes through the deposit of lawful money and on account of $54,980 through the return to the Comptroller for destruction of an equal amount of Federal reserve bank notes.

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CLEARING AND COLLECTION.

As explained in the report of last year, the Board found that the introduction of a general and effective clearance and collection system was a highly technical matter, involving legal questions and many complexities of practice. It was calculated to arouse the opposition of many banks, due to the loss of revenue from the exchange which they had been accustomed to charge for remittances. The Board at first thought best therefore, to leave the actual initiative in the matter largely to the Federal reserve banks, and at their instance to authorize a voluntary system of clearance and collection in which member banks might or might not participate, as they might prefer. Such a system, as explained in the Board's annual report of 1915, was, in fact, inaugurated, and for a time it was hoped that it would prove at least moderately successful. Experience, however, soon showed that many factors were militating strongly against this system. The number of members did not increase materially, and in some districts declined. There were conditions which indicated that the existence of the system in the form

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then adopted was a hardship to certain classes of banks, while the plan did not attain, and seemed unlikely ever to reach, such a plane of efeiciency as to make it a general factor in the clearance and collection system of the country. For these reasons it was decided by the Board during the month of April, 1916, to establish a more comprehensive and uniform system, and it consequently adopted a plan of clearing and collection, informing the several Reserve Banks that they were expected to put it into effect. It was originally intended to begin operations under the new plan on June 15, but subsequent events made it desirable to defer this date for a month, so that it actually became operative on the fifteenth of July,. Under the new system member banks, as long as they comply with the statutory requirements, may continue to carry accounts with their present correspondents and with other banks to whom they may send items for collection, and from whom they may receive for similar purposes, checks drawn upon themselves or upon other banks. They are, however, required to pay without deduction checks drawn upon themselves and presented at their own counters. Remittance of such

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checks by the Federal reserve bank of their district through the mail, is construed as presentation at their own counters, and they must settle with the Federal reserve bank for such checks, either by acceptable checks upon other banks, or by remittance of lawful money or Federal reserve notes at the expense of the Federal reserve bank, in case they are unable to send in offsetting checks on other banks. Checks drawn upon a member bank which have been received by the Federal reserve bank, are not charged against its reserve account until sufficient time has elapsed for the checks to have reached the member bank and for returns to have been received in due course by the Federal reserve banks.

The Board's clearing plan provided also that a small service charge (from one to two cents per item) be made at stated intervals against such banks as send to the Federal reserve bank checks on other banks for collection and credit; but it follows that no portion of this charge can be assessed against any bank unless it shall have elected to avail itself of the facilities offered. Federal reserve banks handle, beside checks drawn on member banks, checks on such State banks as can

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be collected at par, and member banks desiring to handle for a Federal reserve bank checks drawn on State banks, are given the preference. During crop-moving periods it is thought that this will be a distinct advantage to member banks.

There is no disposition to deprive member banks of any income that they have been in the habit of receiving from the collection of drafts (other than bank checks) or from the purchase or discount of commercial bills of exchange, and so there should be no diminution in the customary profits of member banks from such sources.

It was estimated that as soon as the new clearing system could be put into operation, checks upon about 15,000 national banks, State banks, and trust companies throughout the United States, could be handled by the Federal reserve banks at par, subject to the small service charge above referred to; and as a minority of the banks would find it difficult to retain much of their most desirable business when checks drawn upon them are at a discount, while checks drawn upon the majority of banks can circulate at par, it was thought that in the near future checks upon

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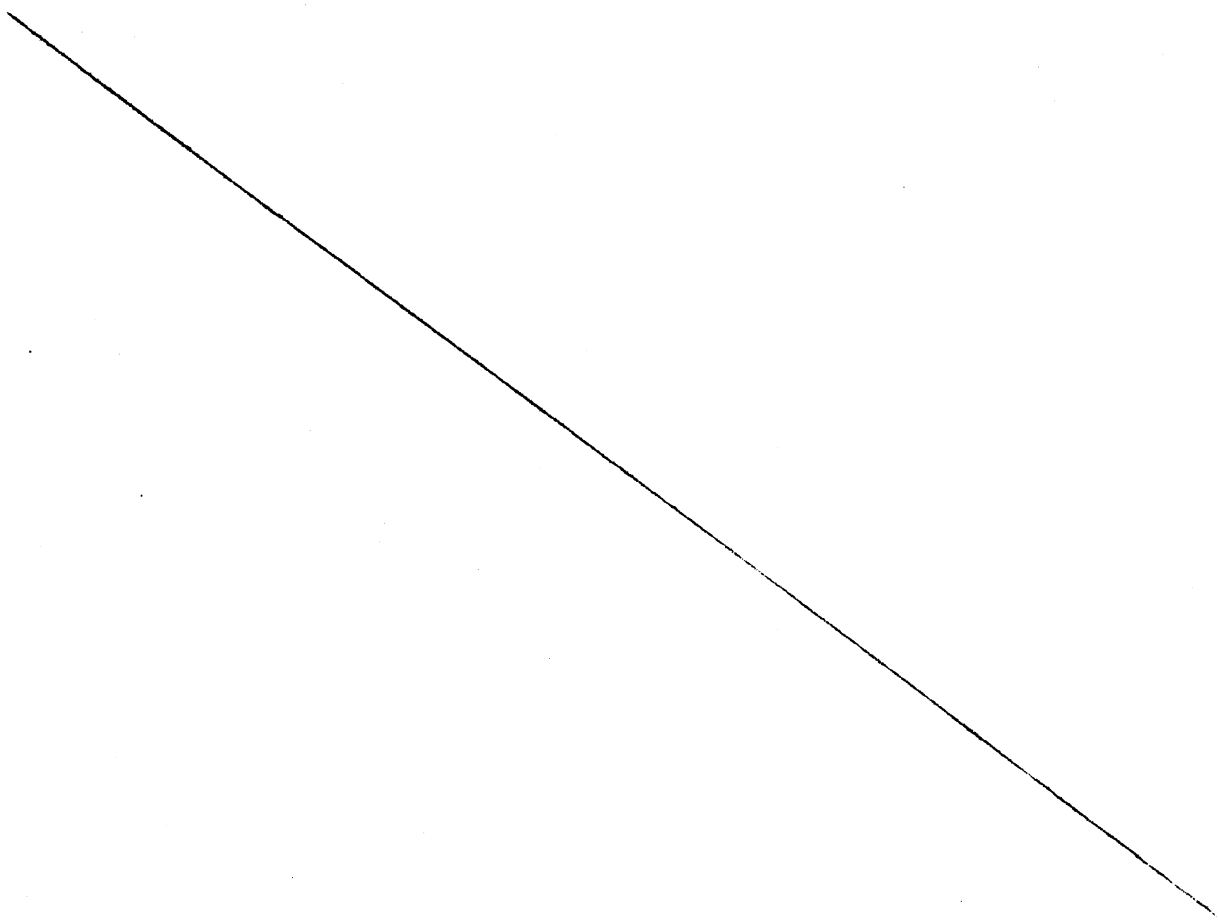
practically all banks throughout the United States could be handled at par by Federal reserve banks. Many banks have found it necessary hitherto to maintain balances with a number of correspondents for exchange purposes, thus compelling them to keep excessive balances away from home. Under the new plan the number of banks upon which par collections are being made, was on December 15, over 15,000; while in other respects the system is developing as anticipated. The total daily clearances at all Federal reserve banks are now over $125,000,000.

After November 17, 1917, or sooner, should the proposed amendment be adopted, no bank balance will be available as reserve for national banks except balances in Federal reserve banks, and, therefore, after that time any necessity to maintain non-reserve balances with correspondents, either for exchange purposes or in order to obtain collection facilities, would be deemed in many cases a great hardship. It is believed that in numerous instances banks will find it expedient to concentrate their balances and to close many accounts which they now carry with other banks, and that a system which will enable them to send

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all of their checks on other banks to the Federal reserve banks for exchange purposes, or as an offset against checks on themselves forwarded by the Federal reserve banks, will, in course of time, come to be appreciated as a convenience.

The following table shows briefly the clearing operations of the Federal reserve system for the monthly period ending December 15, 1916, with comparative figures for each of the four preceding months:



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OPERATIONS OF THE FEDERAL RESERVE INTERDISTRICT CLEARING SYSTEM

November 16 to December 15, 1916.

Bank.	Average number of items handled daily.	Average amount of daily clearing	Member banks in the District	Nonmember banks from which checks are collected at par.
Boston	38,479	$13,153,317	402	242
New York	42,551	28,307,438	625	313
Philadelphia	30,081	16,545,774	632	292
Cleveland	15,873	8,320,355	754	496
Richmond	17,064	8,062,500	520	286
Atlanta	13,851	4,689,214	390	440
Chicago	(a)20,452	13,220,268	993	1,269
St. Louis	10,039	8,402,904	469	881
Minneapolis	15,613	8,828,269	759	1,100
Kansas City	13,782	7,791,296	941	1,412
Dallas	12,734	6,521,235	621	238
San Francisco	5,519	1,761,162	521	1,096
Total Nov. 16 to Dec. 15	236,038	125,603,732	7,627	8,065
Oct. 16 to Nov. 15	227,489	115,061,224	7,623	8,059
Sept.16 to Oct. 15	204,891	97,666,107	7,618	7,459
Aug. 16 to Sept.15	177,397	78,559,704	7,618	7,449
July 15 to Aug. 15	133,113	59,301,696	7,624	7,032

(a) Does not include Government checks averaging 2,062.

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With the view of making the clearing and collection system more effective and of enabling checks drawn upon nonmember banks and trust companies to be handled by Federal reserve banks in the same manner as checks drawn upon members, the Board has asked that Section 13 of the Act be amended so as to allow Federal reserve banks to receive accounts for collection and exchange purposes from such nonmember banks and trust companies as will agree to remit to Federal reserve banks at par for checks drawn upon themselves, and which will, in addition, maintain a compendating balance with the Federal reserve bank in an amount to be determined by the Reserve bank. This will greatly extend and improve the service and will make the clearing system a comprehensive and all embracing one.

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BRANCHES AND AGENCIES OF FEDERAL RESERVE BANKS.

Of the constructive sections of the Federal Reserve Act Section 3, which provides for the establishment of branch banks, is the shortest. It is as follows:

> "Each Federal reserve bank shall establish branch banks within the Federal reserve district in which it is located and may do so in the district of any Federal reserve bank which may have been suspended. Such branches shall be operated by a Board of directors under rules and regulations approved by the Federal Reserve Board. Directors of branch banks shall possess the same qualifications as directors of Federal reserve banks. Four of said directors shall be selected by the reserve bank and three by the Federal Reserve Board, and they shall hold office during the pleasure, respectively, of the parent bank and the Federal Reserve Board. The reserve bank shall designate one of the directors as manager."

In its annual report for 1915 the Board stated that only in one instance did it receive a definite request from a Federal reserve bank to establish a branch. This refers to the application of the Federal Reserve Bank of Atlanta to establish a branch in New Orleans. Up to this time no other Federal reserve bank has asked the sanction of the Board for the establishment of a branch. The expense incident to the operation of a branch is no doubt a deterrent, and while the terms of

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Section 3 appear to be mandatory as to the establishment of branch banks, it will be observed that no time is specified within which they must be established. While it has been intimated to the Board that there are a few cities in some of the districts that would like to secure a branch of the Federal reserve bank, the only application that has been presented to the Board has been one from the bankers of the city of Louisville, asking that a branch of the Federal Reserve Bank of St. Louis be established there. A committee representing Louisville bankers, appeared before the Board on December ____ and presented arguments to support their application, but so far no action has been taken by the Federal Reserve Bank of St.Louis, and the Board has reached no conclusion in the matter. The New Orleans branch of the Federal Reserve Bank of Atlanta was established after a specific request had been made by the board of directors of the Atlanta bank. In accordance with this prece-

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dent, and in view of the provision of law which requires the Federal reserve banks to establish branches, without giving the Federal Reserve Board any direct authority in the matter except to approve rules and regulations under which the branches shall be operated, the Board has doubted the propriety of taking steps to establish branches until the movement had been initiated by the Federal reserve banks. When the branch bank in New Orleans was established, member banks in Louisiana, in Mississippi, and in two counties in Alabama, were advised that they had been assigned to the New Orleans sub-district, and that their reserves should be kept with the branch bank at New Orleans, and that all of their transactions with the reserve bank should be conducted through it. The amount of the capital stock in the Federal reserve bank of Atlanta held by the member banks assigned to the New Orleans branch is regarded for bookkeeping purposes as the theoretical capital. The profits arising from the discount of paper for

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member banks from the purchase of commercial paper and bills of exchange andfrom transfers of funds are shown on the books of the branch bank from which are deducted all expenses of operation. The income and expenditures of the branch bank, however, appear each day on the balance sheet of the parent bank. During the year 1916 the gross earnings of the branch bank at New Orleans were $62,052, and the total expenses of operation, including salaries of employes, and directors' fees, amounted to $28,645, leaving a net profit to the Federal Reserve Bank of Atlanta from the operations of its New Orleans branch of $33,407, which profit amounts to 7.5% on the theoretical capital of $445,000 allotted to the New Orleans branch.

It is fair to assume that a portion at least of these profits would have accrued to the Federal Reserve Bank of Atlanta had there been no branch at New Orleans. In view of experience gained from the operation of the one branch bank in the entire system, it seems that it would be wise, in considering the establish-

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ment of other branches, to take into account whether they would be really self-sustaining, i. e., whether the net profits growing out of their operation would exceed the revenue that would accrue in any event to the parent bank.

While the Board has not deemed it necessary at this time to ask for an amendment of Section 3, it will probably be well, before branches are established generally, to ask for legislation to simplify their operation, and to reduce the cost of maintaining them.

The Board has been informed that many of the Federal reserve banks are ready to establish agencies or offices in such cities in their districts as may require special services, such as the collection of checks or the making of loans on warehouse receipts. An agency of this kind was established by the Federal Reserve Bank of St.Louis in September last, at Memphis, Tennessee, and it has proved convenient to the banks of that city in the handling of the cotton crop.

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OPERATIONS ABROAD.

The Clearing and collection system has now fairly begun its potential activities, and it has demonstrated that the provisions of the Federal Reserve Act relating to this feature of the business of Federal reserve banks, are feasible and practical; and it is confidently expected the present year will witness a general acquiesence in it and its use by all banks. With the completion of the collection and clearing system, all the domestic functions of Federal reserve banks will have been at lease tentatively undertaken, requiring only a reasonable period of development for their complete application. With regard to the provisions of the Federal Reserve Act relating to foreign trade, the case is different. While much has been done to facilitate the financing of foreign trade through the development of the acceptance market and by the establishment abroad of American banks, the providions of the Act call for the establishment of foreign agencies or branches of Federal reserve banks have not as yet been put into operation, nor have the reserve banks undertaken the direct purchase of foreign commercial bills,

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or the performance of other functions relating to foreign transactions authorized in the law. This dealy has been due partly to the disturbed condition of business in markets, abroad, and partly to the belief that a sound and thorough application of the law in its domestic aspects should naturally precede the undertaking of foreign operations allowed by the Act. The Board has, however, had under consideration for some time, the advisability of authorizing Federal reserve banks to appoint correspondents, and to establish agencies in foreign countries, and on December 20th formally approved the application of the Federal Reserve Bank of New York for authority to establish an agency with the Bank of England. This authority was granted under the provisions of Section 14 of the Act which permit any Federal reserve bank "with the consent of the Federal Reserve Board to open and maintain banking accounts in foreign countries, appoint correspondents, and establish agencies in such countries wheresoever it may deem best for the purpose of purchasing, selling and collecting bills of exchange and to buy and sell with or without its endorsement through such correspondents or agencies

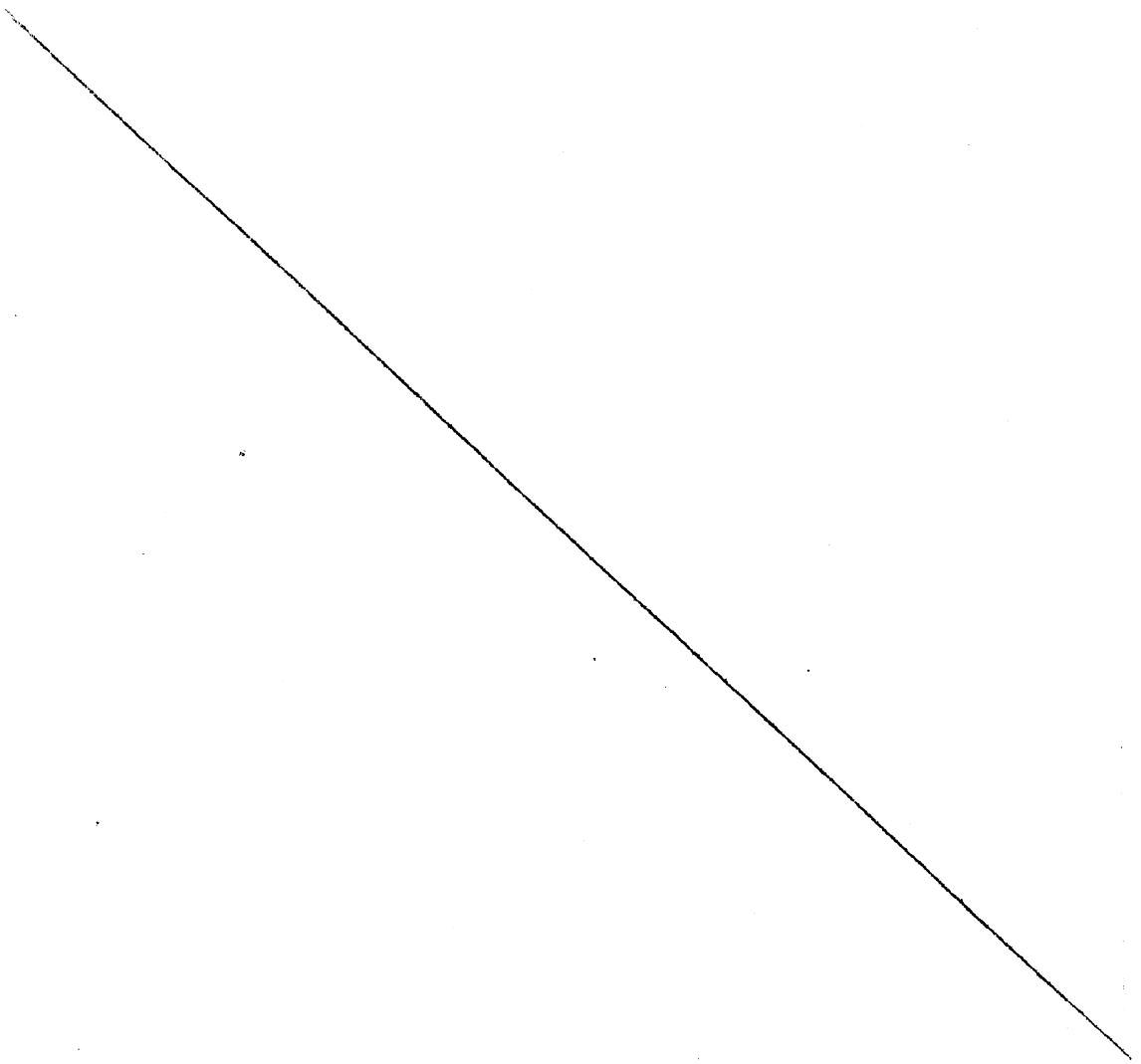
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bills of exchange arising out of actual commercial transactions," so that a broad field of operations is opened under it. Other Federal reserve banks may participate in the agency relationship with the Bank of England upon the same terms and conditions that will govern the Federal Reserve Bank of New York, if they so desire.

Other connections of this character will probably be authorized from time to time as occasion requires, thus giving full effect to that section of the Federal Reserve Act which seeks to relieve our banking system of its old-time restrictions and to extend its usefulness to the promotion of f foreign trade on favorable terms. Hitherto banking operations connected with foreign trade have been almost entirely in the hands of trust companies and private bankers, but as far as the future is concerned, there seems to be no reason why the Federal reserve banks should not be placed upon practically the same

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footing as the great Governmental banks of Europe, and given wide powers in the matter of international exchange, with the Federal Reserve Board acting as the central controlling force in the coordination and direction of operations.



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ENFORCEMENT OF THE CLAYTON ACT.

Important duties relative to the determination of the eligibility of member bank directors, were laid upon the Federal Reserve Board by the amendment to the Clayton Act, known as the "Kern amendment", which became a law on May 15, 1916. This legislation was intended to provide for an enlargement of the powers of individuals in accepting and holding bank directorates. It authorized such individuals, when directors of member banks, to act also as officers, directors or employes of not more than two other banks, banking associations, or trust companies, when organized under the laws of the United States or any State, "if such other bank, banking association or trust company is not in substantial competition with such member bank." It was, however, required that the consent of the Federal Reserve Board be obtained as a basis for the continuance of such relations with other banks. This threw upon the Board as a condition necessarily precedent to the granting or withholding of its consent in

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such cases, the duty of ascertaining whether the banks in which an individual might seek to hold directorships, were or were not in substantial competition with the member bank of which such individual was also a director. A special committee of the Board passed in review the various applications filed with it, this work occupying a considerable part of the time during the months of August, September, and the first half of October; - the Clayton Act by its own terms becoming effective on October 15. During the period in question the Board considered in all 1335 applications of which 1195 were granted, and 140 refused. In a large number of additional cases the directors affected undoubtedly recognized that substantial competition did unquestionably exist and so withdrew from one or more directorships, thereby bringing themselves in compliance with the Act without any appeal to the Federal Reserve Board. A difficult element was found in the provisions of the Clayton Act which prohibit a private banker from holding a directorship in a member bank. Compliance

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with this prohibition necessarily involved a definition of the term "private banker", and the Board accordingly agreed upon such a definition for its own guidance in passing upon applications. The term private banker was interpreted to include partnerships or individuals engaged in the banking business, as the term is generally understood, including those partnerships or individuals who solicit or receive deposits subject to check, who do a foreign exchange, acceptance, loan or discount business, or who purchase and sell or distribute issues of securities by which capital is furnished for business or public enterprise. The term was thus interpreted not to include the ordinary stock, note or commodity broker unless a substantial proportion of his profits comes from banking activities, nor did it include partnerships or individuals using only their own funds in making loans or investments.

In a number of cases difficulty was encountered in determining the exact scope properly to be assigned to the term "substantial competition", particularly with reference to the

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question whether such competition must be regarded as limited in area. It was found that some large banks competing with one another over a given area did not compete throughout the whole field of their business, some of them being national in scope, while others confined their activities much more narrowly. While in some instances it was thought best to grant the applications of directors who were desirous of serving on the boards of such banks, it was indicated in each case that the consent accorded to them was tentative only, and that further investigation would be undertaken for the purpose of arriving at a final conclusion. Indeed the whole of the Board's work with reference to the application of the Kern amendment must be regarded as unfinished. New facts or evidence bearing upon the business of given institutions may at any time develop, or the natural growth of the business of given institutions may be such as to bring them into substantial competition, although

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they were not previously regarded as being so. It will, therefore, naturally be necessary from time to time to revise the decisions already made, or conditions may develop such as to necessitate the revocation of the permission already granted in certain cases, in order to deal appropriately with new conditions, without, at the same time, subjecting some directors to a rule different from that applied in the case of others. As in all new legislation, there is a considerable zone of uncertainty in the interpretation and application of the Clayton Act. It will require experience and further analysis to overcome such uncertainties and to apply the terms of the measure fairly and uniformly, while carrying out the essential intent of Congress.

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ENTRY OF NEW MEMBERS.

During the year 1916, 113 banks entered the Federal Reserve system, making a total of 7,635 members on December 31, Of these new members 60 were newly organized national banks, which, under existing law, automatically became members and took out stock in the Federal reserve bank of the district in which they were located. Of the remaining new members, 48 were State banks which entered the system through their conversion into national banks, thereupon automatically becoming members. State institutions which applied for and received membership, while retaining their State charters, numbered 7. It had been supposed that upon the organization of the clearing and collection system, a considerable number of State institutions would find it to their advantage to apply for membership, or that other factors would tend to bring them into the system. So far this has not proved to be the case, for the number of State institutions which came into the system during 1916 while retaining their local charters, was less than during the preceding year. Many causes have operated to produce this result, the chief being those

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already outlined by the Board in its report for 1915. Added to these considerations has been the effect of the Clayton Act, which is objected to by many State banks as likely to result in inconvenient or undesirable changes in their boards of directors should they affiliate themselves with the Federal reserve system; and the operation of Section 22 of the Federal Reserve Act, which deals with the relations of directors of member banks to their institutions. The Board has suggested an amendment to this section designed to clarify it and to remove uncertainties, without affecting in any way its principle.

Apprehension of stringent conditions or the development of any situation requiring mutual aid on the part of banks, would undoubtedly cause many nonmember banks to apply for membership, but it is not believed that they will, as a rule, elect to await such conditions. There are some indications that several important institutions are awakening to a sense of public duty in the matter, and are besides, gradually reaching the conclusion that their own best interests require their affiliation with the Federal reserve system.

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Many apprehensions, previously entertained have been shown to be groundless, and the attitude of the board toward State banks as members is better understood than formally.

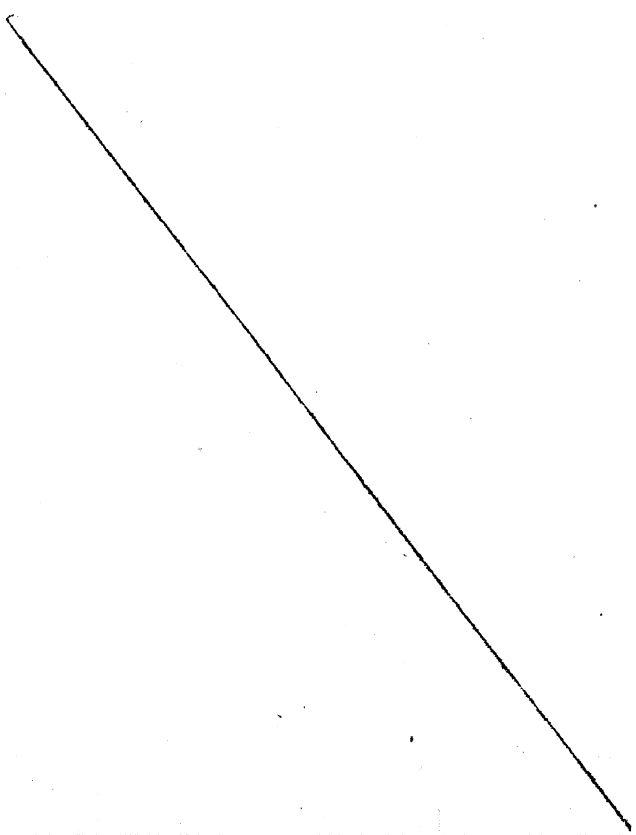
In July last the Board advised the representatives of certain State banks and trust companies which were apprehensive that membership in the system might involve an undue restriction of their corporate activities as a result of the future regulations of the Board, that it did not understand that it was incumbent upon it to undertake to impose on the activities of member banks any restrictions that are not contemplated by the Act, but only to prescribe such regulations as are designed to carry out the purposes of the Act, The Board does not feel that it is one of its functions to undertake to restrict State banks or trust companies in the exercise of banking or trust company powers as defined by the laws of the State in which they are created. In passing upon the applications of State banks and trust companies however, the Board holds that it would be its duty to admit only those institutions which are

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solvent and sound and whose membership will not constitute an element of weakness in the system. The Board does not consider that it is a prerequisite to the admission of any State bank or trust company that it should possess any certain amount of paper eligible for rediscount with a Federal reserve bank. The law provides that privileges and advantages of membership may be extended to State banks and trust companies, thus contemplating one compact banking system, while preserving the integrity of both the State and the National banking systems. The fact that a State bank has little eligible paper does not of itself make its membership an element of weakness or danger, and it is obvious that as a member of the system it will be in a position to contract for loans and to obtain cash from other member banks having paper eligible for rediscount, and thus indirectly to obtain desired accommodations. The ability to assist member banks directly and indirectly will be increased as the strength of the system and lending power of the Federal reserve banks are increased. There is no reason why such assistance should not be

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given freely to a member State bank, while in time of stress the non-member banks may find the member banks not less disposed but less able to give them this indirect assistance. The Board of course might consider the exercise of extraordinary and unusual powers, such as make an applying State bank or trust company an undesirable member, a sufficient reason to refuse to grant the application for admission, but after a State bank or trust company has actually become a member bank, the Board does not expect to interfere with the exercise of those banking and fiduciary powers authorized by its charter.



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FIDUCIARY POWERS.

Applications for permission to exercise fiduciary powers under the terms of the Federal Reserve Act have continued to be presented to the Board during the past year, and have been granted in 110 cases, action on 77 of which carried approval of full fiduciary powers, while in the case of 33 limited powers only were granted. The falling off in the matter of applications as compared with the year 1915, was probably due to uncertainty as to the legal status of the banks in exercising this function, the doubts regarding it having been intensified by the action of the Supreme Court of the State of Michigan in handing down, on September 26, an opinion adverse to the contention of the national banks.* It was the view of the court in this case

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*Grant Fellows, Attorney General of the State of Michigan, on the relation of the Union Trust Company, Detroit Trust Company, Security Trust Company, Michigan Trust Company, and the Grand Rapids Trust Company, vs the First National Bank of Bay City.

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that Congress had no authority to permit national institutions to exercise the fiduciary powers provided for in the Federal Reserve Act, and, in accordance with the policy announced in its report for 1915, the Board took steps to have the case transferred to the Supreme Court of the United States on a writ of error, in order that an authoritative decision might be finally rendered. In the meantime the Board is pursuing the policy of granting to properly qualified and well-managed banks the authority to exercise fiduciary powers in so far as provided by the Federal Reserve Act. As has been explained on former occasions, the Board cannot do less than grant specifically the powers that have been bestowed generally by Congress under the Federal Reserve Act; and in making such grants, the Board merely carries out the duties imposed upon it by the Act, leaving it to judicial interpretation how far and to what extent the powers in question may legally and constitutionally be exercised. It will, in the natural course of events, be some time before this issue can be finally disposed of, and in the meanwhile the Board will continue to pursue its present course of action.

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CHANGES IN DISTRICTS.

In its report for 1915 the Board set forth the reasons that had led it to make certain changes in the boundaries of Federal reserve districts, and it was there stated that "further consideration of this subject was suspended in view of an opinion rendered by the Attorney General of the United States * * * wherein it was held that the Board possessed no power to reduce the number of Federal reserve districts." The Board also called attention to the fact that "a further opinion has been asked as to whether the Board has power to change the location of a Federal reserve bank within a district." The opinion thus referred to was rendered by the Attorney General on April 4, 1916, and covered two points -

(1) Whether the Board could change the present location of any Federal reserve bank in certain cases, and

(2) Whether the Board in readjusting district lines must preserve the $4,000,000 minimum capitalization required of each Federal reserve bank.

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The Attorney General held that the Board has no power to change the location of a bank, irrespective of alterations or readjustments in district lines, but that the maintenance of the minimum capitalization of $4,000,000 was not necessary.

The effect of this ruling was to eliminate from further consideration the pending appeals which involved changes in the location of Federal reserve banks within their districts. In view of the opinion of the Attorney General there remained but three appeals calling for immediate decision - that filed by certain Connecticut banks which requested transfer from the Boston to the New York District; that filed by certain banks in Wisconsin which requested transfer from the Minneapolis to the Chicago District; and that filed by certain banks in southern Louisiana which requested transfer from the Dallas to the Atlanta District. The Louisiana appeal was granted by a resolution adopted on February 25th transferring certain banks as desired; while the Connecticut appeal was determined by a resolution on March 6th transferring these banks

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banks situated in Fairfield County, Connecticut, to the New York District, leaving the remainder of the Connecticut banks as members of the Federal Reserve Bank of Boston. The Wisconsin appeal was settled by an order of October 12th, transferring the applying banks in central and eastern Wisconsin to the Chicago District.

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OPERATION OF THE BOARD.

On August 10, 1916, the Federal Reserve Board had been in existence two years, and, under the provisions of the Act creating it, the term of one member came to a close two years after his original appointment. On July 25 the President sent to the Senate the nomination of Honorable Charles S. Hamlin to succeed himself as a member of the Board, the appointment being for a term of ten years. This nomination was confirmed on August 3. Mr. Hamlin's term under his earlier appointment expired on Wednesday, August 9. He qualified by taking the oath on August 10. Honorable W. P. G. Harding was, on August 10, designated by the President of the United States as Governor, and Honorable Paul M. Warburg as Vice-Governor of the Board, both "for a period of one year, or until otherwise directed."

The Federal Advisory Council has held its four stated meetings during the last year, and has discussed topics submitted to it by the Board, as well as questions raised by its own members,

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presenting results of the discussions to the Board. A report of the proceedings of the Council is appended hereto as Exhibit "_____". Conferences were held also by the Federal reserve agents on May 29 and December 4, in Washington, the time at these meetings being devoted to the consideration and analysis of questions of current interest to the Federal reserve banks. The meetings of Governors of Federal reserve banks which have taken place at intervals since the organization of the system have continued, three such meetings having been held during the year.

The staff and internal organization of the Board have continued without important modification, the principal changes being the better development of its organization, and the gradual growth and enlargement of the work. The personnel and size of the staff remains essentially unaltered, and the cost of conducting the Board's work, including members' salaries and the total outlay at the offices in Washington, inclusive of the corps of

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examiners, is still about $180,000 per annum -- the estimated figure mentioned in the report for 1915. The Gold Settlement Fund, to which reference has been made elsewhere in this report, has greatly enlarged the volume of its clearing, but without corresponding increase in expense of operation, the cost for the year 1916 being about $2,500, while the total volume of business cleared during the year has been about $8,000,000,000. The Gold Settlement Fund was originally conducted merely as a means of settling between Federal reserve banks, but its scope of operations has been enlarged by providing a similar fund for Federal reserve agents, conducted on the same plan as the Gold Settlement fund itself. This renders possible the making of payments not only between Federal reserve banks, but also between the reserve agents and their own banks, without the necessity of shipping gold or its equivalent back and forth.

The Federal Reserve Bulletin has been conducted throughout the year as during the year 1915, as a monthly publication.

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and has been enlarged in size, and broadened in scope in response to the increasing public interest. It is distributed free of charge to all member banks, but it has also a growing list of paid subscribers among non-members and the financial community generally. So fully has the Bulletin dealt with all of the details of the operation of the Federal reserve system, that it is unnecessary to repeat them in this report, a complete file of the Bulletin itself being transmitted as supplementary to the information herein given.

EARNINGS AND EXPENSES.

The past year has shown a very decided improvement in the income-earning power of the Federal reserve banks. They have been able to provide for their expenses and to carry a substantial amount to dividend account. For the year 1916, as will be seen in greater detail from figures furnished in the exhibits to this report, the current expenses of the system were $_____,

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while the total net earnings for the entire year were $_____ The following table shows the dividend declared by Federal reserve banks from the date of their organization down to the present time:

(Insert table)

The figures for the whole system to the end of 1916 show an average net earning since their organization of _____% on the capital actually involved, while for the year 1916 they show an average net earning of _____%. The advance in earning power thus shown is especially gratifying when it is remembered that discount rates have continued low, being practically no higher than they were in 1915; while both years have been exceptionally unfavorable for rediscount institutions, owing to the great plethora of funds in the vaults of member banks generally, the consequent low rates of interest and the lack of need for member banks to obtain accommodation.

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The average "rediscounts" of all national banks as shown by five abstracts issued by the Comptroller of the Currency in 1916 were $_____. Of this amount $_____, or _____% were rediscounts with the Federal reserve banks.

The Federal reserve banks have not been operated with a view to profit, but they have all earned their expenses, together with a substantial part of their dividend requirements. They appear to have gained steadily in the confidence of the public, and the fact of their existence has enabled the country to withstand, without the slightest financial disturbance and without any marked fluctuations in rates for commercial paper, many shocks and sensations which probably would, under old conditions, have been followed by unpleasant results. The Federal reserve system is no longer looked upon as an ephemeral experiment. It has been established upon a firm and enduring foundation, and it has been demonstrated repeatedly that it is not being conducted for the particular benefit of any

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group or interest, but that the policies governing its operation are, and must continue to be, broad enough to serve, without discrimination or favor, the banks and those who deal with banks throughout the entire country. While regulatory and conservative, it is none the less a constructive force, and when conditions throughout the world become more normal, the Federal reserve system will be recognized, not only as a dominant factor in our own financial affairs, but as a most important influence in the commerce of the world.

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PROPOSED AMENDMENTS.

The most important changes in the Act that have been suggested by the Board and which relate to note issues and to reserves, have already been discussed at an earlier point in this report under the heading of conservation of gold supply; but for convenient reference we append a complete list of the Board's amendments, the tex of which has been submitted to the proper committees of the Senate and House.

1. Amendment to Section 16, providing

   (a) For the issue of Federal reserve notes directly against the deposit of 100% gold or 100% of paper, or both, the gold reserve in no event to be below 40%.

   (b) For the counting of gold held by the Federal Reserve Agents as security for notes as part of the gold reserve required to be held by the banks against such Federal reserve notes.

This amendment was not agreed to unanimously, but was approved and endorsed by a majority of the Board. Its purpose has already been discussed at length elsewhere in this report.

2. Amendment of Section 19 abbreviating and simplifying the

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clauses in Section 19 which relate to reserve requirements. This proposed amendment provides that all member banks shall maintain reserves in the Federal reserve banks as follows:

	Against Demand Deposits	Against Time Deposits
(a) Country Banks	7%	3%
(b) Reserve City Banks	10%	3%
(c) Central Reserve City Banks	13%	3%

and in addition every member bank is required to keep in its own vault for till money an amount of specie or currency (not necessarily gold or lawful money) equal to five per cent of its demand deposits, less the amount of net balances with Federal reserve banks in excess of the minimum above stipulated.

3. 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

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requirements.

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

4. 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

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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 against discrimination, and it is designed to enable the Federal reserve banks to collect all checks at par, whether they are drawn upon member banks or nonmember State banks and trust companies. Any clearing 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 points that 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

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with the Federal reserve banks. A necessary factor in any sound 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.

5. 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.

6. 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. This feature was in the law but was inadvertently omitted when the Act was amended on September 7, 1916.

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7. 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 FederalmReserve 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.

8. 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

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banks and trust companies from establishing branches.

9. 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 Gederal 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.

10. Amendment of Section 18 so as to give to United States

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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.

11. 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 re-

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serve 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 fee 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.

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1912

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

965.

January 11, 1917.

Federal Reserve Bank,

Gentlemen:

We understand that the weekly reports for the gold settlement fund as forwarded now, represent the credits in a single account which you carry with each other Federal reserve bank. You have, no doubt, considered the desirability of reporting, instead of the credit amount for each account, merely the net amounts in accounts where the balance is in favor of another Federal reserve bank. The obstacle to be encountered in this connection is, of course, the difficulty of having the time schedules so operated as to secure exact agreement at any moment between the accounts of the various banks, but the benefits of reporting the smaller number of items are so obvious that we think it desirable to endeavor to ascertain how closely the various acccunts would agree.

To this end, we request that, in addition to sending the regular weekly telegram as at present, you forward by mail each Wednesday evening for some little time to come, a memorandum of the net amount standing to the debit or credit of each of the other Federal reserve banks. In this way, we can soon determine whether or not a report based on only the net credit balances would be satisfactory.

Very truly yours,

Assistant Secretary.

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Federal Reserve Bank of St. Louis

966 1913

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

January 10, 1917.

Dear Sir:

This will call attention to the fact that copy for business conditions to be used in the Federal Reserve Bulletin, for February should be in the offices of the Federal Reserve Board not later than January 24, 1917. With this copy, please send the usual information as to clearing operations on which the summary for the Bulletin is made up, and do not fail to include the summary of business conditions upon the slips furnished you for the purpose.

Because of the fact that paper and other costs have increased, the Board desires to reduce the size and cost of the Bulletin as much as possible. You are, therefore, requested to limit your statement of business conditions to not more than one thousand words, unless some unusual condition has arisen in your district which warrants an extension of your discussion.

Very respectfully,

Secretary.

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FOR RELEASE IN MORNING PAPERS, JANUARY 14, 1917.

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

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(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

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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 thecry 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

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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-

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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

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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 propostion 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.

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 3 of the Act approved December 23, 1913, known as the Federal Reserve Act, be amended and reenacted so as to read as follows:

> Sec. 3. The Federal Reserve Board may permit or require any Federal reserve bank to establish branch banks within the Federal reserve district in which it is located or within the district of any Federal reserve bank which may have been suspended. Such branches, subject to such rules and regulations as the Federal Reserve Board may prescribe, shall be operated under the supervision of a board of directors to consist of not more than seven nor less than three directors, of whom a majority of one shall be appointed by the Federal reserve bank of the district, and the remaining directors by the Federal Reserve Board. Directors of branch banks shall hold office during the pleasure of the Federal Reserve Board.

1/13/17

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BE IT ENACTED BY THE SENATE AND HOUSE OF REPRESENTATIVES OF THE UNITED STATES OF AMERICA IN CONGRESS ASSEMBLED, That Section 14, subsection (e), of the Act approved December 23, 1913, known as the Federal Reserve Act, as amended by the Act approved September 7, 1916, be further amended and re-enacted so as to read as follows:

(e) To establish accounts with other Federal reserve banks for exchange purposes and with the consent OR UPON THE ORDER AND DIRECTION of the Federal Reserve Board UPON AN AFFIRMATIVE VOTE OF NOT LESS THAN FIVE MEMBERS, AND UNDER REGULATIONS TO BE PRESCRIBED BY SAID BOARD, to open and maintain accounts in foreign countries, appoint correspondents, and establish agencies in such countries wheresoever it may BE deemED best for the purpose of purchasing, selling, and collecting bills of exchange, and to buy and sell, with or without its indorsement, through such correspondents or agencies bills of exchange OR ACCEPTANCES arising out of actual commercial transactions which have not more than ninety days to run, exclusive of days of grace, and which bear the signature of two or more responsible parties, and, with the consent of the Federal Reserve Board, to open and maintain banking accounts for such foreign correspondents or agencies. WHENEVER ANY SUCH ACCOUNT HAS BEEN OPENED OR AGENCY OR CORRESPONDENT HAS BEEN APPOINTED BY A FEDERAL RESERVE BANK WITH THE CONSENT OF OR UNDER THE ORDER AND DIRECTION OF THE FEDERAL RESERVE BOARD, ANY OTHER FEDERAL RESERVE BANK MAY, WITH THE CONSENT AND APPROVAL OF THE FEDERAL RESERVE BOARD, BE PERMITTED TO CARRY ON OR CONDUCT THROUGH THE FEDERAL RESERVE BANK OPENING SUCH ACCOUNT, OR APPOINTING SUCH AGENCY OR CORRESPONDENT, ANY TRANSACTION AUTHORIZED BY THIS SECTION UNDER RULES AND REGULATIONS TO BE PRESCRIBED BY THE BOARD.

1/13/17

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1922

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

FEDERAL RESERVE BOARD 974

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

January 15, 1917.

Dear Sir:

In re UNFIT FEDERAL RESERVE NOTES FORWARDED TO THE TREASURER OF THE UNITED STATES FOR REDEMPTION BY A FEDERAL RESERVE BANK OTHER THAN THE FEDERAL RESERVE BANK OF ISSUE:

In January, 1916, a plan was formulated to permit Federal reserve banks to forward their own unfit Federal reserve notes direct to the Treasurer of the United States for redemption. That plan, however, did not permit a Federal reserve bank to ship to the Treasurer, Federal reserve notes issued by any other Federal reserve bank.

Section 16 of the Federal Reserve Act provides in part that, whenever a Federal reserve bank receives Federal reserve notes issued by another Federal reserve bank such note shall be returned to the Federal reserve bank of issue for credit or redemption. In order to avoid a round-about shipment of Federal reserve notes, first, from a receiving Federal reserve bank to the reserve bank of issue, and then from the bank of issue on to Washington for redemption, the following plan which permits a receiving Federal reserve bank, under power of attorney, to forward unfit Federal reserve notes of another Federal reserve bank direct to the Treasurer for redemption, has been approved by the Treasury Department and the Federal Reserve Board.

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1. Each Federal reserve bank shall give to each other Federal reserve bank a power of attorney authorizing such other bank to act as its agent in forwarding any of its unfit Federal reserve notes to the Treasurer of the United States for redemption. This power of attorney may be in any form agreed upon by the respective Federal reserve banks and may define the standard to guide the forwarding bank in determining what Federal reserve notes of the issuing bank shall be considered unfit. The forwarding bank shall, at the time of shipment, notify the issuing bank that the shipment has been made for and in its name to the Treasurer, and shall charge the account of the issuing bank for the amount of notes thus shipped. The issuing bank shall then credit the account of the forwarding bank, and shall increase on its books the item, "Mutilated Currency forwarded for redemption" just as if it, itself, had sent unfit notes direct to the Treasurer for redemption.

2. The Treasurer, on receiving such notes, will advise the forwarding banks of their receipt.

3. The Treasurer will then complete the transaction just as if the notes had been forwarded to him for redemption direct by the bank of issue, under the plan approved by the Treasury Department and the Federal Reserve Board in January, 1918. In accordance with the provisions of that plan, the Treasurer will immediately advise both the Federal reserve bank of issue and its Federal reserve agent of the receipt of the notes sent to him for redemption, and will redeem the notes for the account of the bank of issue, not for the account of the forwarding bank.

4. After the notes have been redeemed the Treasurer, acting under the powers of attorney provided for in the plan, governing the redemption of unfit notes shipped direct by the Federal reserve bank of issue, will forward such notes to the Comptroller of the Currency for cancellation and destruction, advising the Federal reserve agent of this action.

By way of illustration, a specific transaction would be conducted as follows:

(a) The Federal Reserve Bank of Richmond receives from one of its member banks a deposit of unfit notes of the Federal Reserve Bank of Chicago.

(b) Acting under the power of attorney given to it by the

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Chicago bank, the Richmond bank forwards these unfit notes to the Treasurer for redemption for and in behalf of the Chicago bank.

(c) As soon as the Richmond bank makes the shipment described in paragraph (b) it charges the account of the Federal reserve bank and so notifies Chicago.

(d) Upon receipt of the notice forwarded under paragraph (c) Chicago credits the account of the Richmond bank and increases on its books the item "Mutilated currency forwarded for redemption".

(e) The Treasurer, on receipt of the notes shipped by Richmond, will acknowledge receipt to Richmond, will advise both Chicago and its Federal reserve agent simultaneously that the notes have been received for the account of the Chicago bank, and will redeem such notes just as if they had been sent by the Federal Reserve Bank of Chicago direct to the Treasurer for redemption.

(f) Upon receipt of the advice forwarded by the Treasurer, as provided in paragraph (e) the Federal Reserve Bank of Chicago and its Federal reserve agent will record the transaction in the manner outlined in a circular letter from the Board dated March 24, 1916, hereto attached.

(g) When the notes have been redeemed the Treasurer will deliver them to the Comptroller of the Currency in the name of the Federal reserve agent at Chicago and for his credit.

(h) The Comptroller of the Currency, upon receipt of the notes from the Treasurer, will notify the Federal reserve agent that they have been received for destruction, will arrange for their cancellation and destruction, and will credit the account of the Federal reserve agent of Chicago with the amount of the notes when destroyed.

Very truly yours,

Governor.

Inclosure.

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Federal Reserve Bank of St. Louis

1925

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
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ADOLPH C. MILLER
CHARLES S. HAMLIN

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD
915.

January 15, 1917.

Dear Sir:

Your especial attention is called to the enclosed copy of a form and resolution to be used by member banks in offering for sale United States bonds thrcugh the Treasurer of the United States. The form and resolution attached are those required by the Treasurer.

This notice is sent you because of the fact that one Federal Reserve Bank has sent out a form under which the Treasurer is unable to make the sale of bonds, and to prevent your falling into a similar error.

Especial attention is called to the request that Treasury receipts accompany bonds offered for sale.

Very truly yours,

Secretary.

Enclosure.

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Federal Reserve Bank of St. Louis

1926

REMARKS OF H. P. WILLIS,

At Boston, January 16, 1917.

Mr. Chairman, and Members of the Boston Chapter of the American Institute of Banking:

I have been the guest of the Institute of Banking at many of its chapters East and West in the United States, but never, I think, in Boston. My experience at these meetings has been so happy, that to add another to the list of chapters I have known is always a temptation difficult to resist. In this case your invitation has found me in a receptive mood because you have asked me to tell you what I think about some matters which have long been a favorite subject of study with me, and in which I have lately had some direct experience. Interesting as the Philippine National Bank and the whole question of Philippine trade is in and of itself, its largest interest is found in this - that it is but one phase of a great problem by which the United States is confronted today. I shall refer to the Philippine National Bank and its experience therefore merely to afford practical illustration of my general thought on the broader question.

For many years past American merchants and manufacturers have been talking of export trade. Associations have been formed, meetings frequently held, and valuable ideas expressed. Government bureaus have dilated at length upon reasons why American manufacturers never secured satisfactory control of foreign markets, and Government agents

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have traveled all over the world inquiring into the reasons why we did not sell more of our goods to the natives of distant regions. There had been very little result from all this discussion and investigation until the breaking out of the European war, when many consumers throughout the world who had previously gone for their supplies to producers who studied their needs and undertook to supply them, turned to the United States, not because they wanted to do so, but because there was no choice. Now we have built up a great foreign trade, amounting for the year which has just ended to not less than $5,400,000,000 in exports, and more than $2,300,000,000 in imports, a net balance many times that ever realized in any preceding year. This immense export trade consisted to the extent of 50% of manufactured goods, and while there has been some complaint of the quality of what we have turned out, I think it is safe to say that the goods have given general satisfaction, not withstanding that they have often been regarded as high-priced. Our trade with the Philippines and the Far East furnishes an example of what has occurred that is very interesting, the more so because of the fact that we have a special relation to the Philippine Islands. They are both a foreign country and a part of our territory. Perhaps you are not particularly interested in the Philippine Islands. You have been hearing of them for a long time from the political standpoint. They are a serious and important national problem in that connection. I am not here to deal with them in any such aspect. What I wish to call to your attention is their trade and their relation to our business. The Philippine Islands have today about 9,000,000 people, and their total trade with other countries consisted during the year 1915 of about $103,000,000

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of which $54,000,000 was exported, while $49,000,000 was imported. Of these imports about 53½% came from the United States, while 44% of the exports were sent to the United States. Ten years previously, in 1915, the total trade of the Islands was less than two-thirds what it is today, the exports to all countries amounting to $33,000,000, while the imports from all countries were $30,000,000, approximately. Of the $33,000,000 of exports at that time, a little more than 40% was shipped to the United States, while of the imports into the Philippine Islands, only about 18% came from the United States. During the year 1916 the total value of shipments of domestic merchandise to the Philippines from this country will, it is estimated, aggregate about $22,000,000, while our imports from the Islands may be estimated at $34,000,000. It is worthwhile to study with some care and detail the conditions under which this trade has been developed. Full justice ought to be done to the efforts of manufacturers and shippers in meeting the needs of the native population, particularly as the problem of insular trade is in principle the same as the problem of foreign trade elsewhere. This problem includes the following principal elements:

Desire on the part of American manufacturers to supply goods acceptable to buyers, and the making of transportation of other arrangements needful to the cheap and satisfactory delivery of their goods.

Development of buying power and demand for American goods among foreign consumers.

Establishment of profitable and mutual trade relations so that exports go from the United States by way of payment for imports.

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Creation of economical banking connections.

For many years these elements in the problem have been neglected in the discussion of American-Philippine trade, but today some of them are accepted, and export and import business is steadily improving. A great obstacle to the full development of business has been found in the transportation situation, which, of course, has been bad all through the European war. In spite of this handicap, trade is generally admitted to be in a very promising and satisfactory state. The sugar industry at present is highly profitable wherever modern machinery has been installed, as it has at a number of points in the Islands. Substantial interest in the sugar business is being shown by outside investors, and there is reason to expect that in the near future there will be a considerable development of modern sugar mills equipped with proper machinery and able to produce good centrifugal sugar for export. The cocoanut oil industry is also showing marked development, the business of extracting oil on the spot having been recently introduced in place of the older method of shipping the copra abroad for extraction of the oil. The cigar business has been greatly stimulated by the high prices of tobacco in Europe and the United States. Hemp is high in price and, as usual, is in strong demand. In consequence of the good prices realized for their products the natives have become better customers than in the past, and their desire for American goods of all kinds makes the Islands a desirable market for textiles, automobiles, sewing machines, iron and steel products of all kinds, various forms of wearing apparel (particularly shoes), canned goods, and a great variety of manufactures, especially those which have a relatively large value in small bulk, and hence are able to bear comparatively high rates of freight.

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Americans in trading with the Philippines have committed the error of supposing that a large part of their market would depend upon the growth of an American colony in the Islands. They are now finding it more profitable to adapt themselves to the native demand. Our exporters are thus at last seemingly working along somewhat the right lines, although they are treating the subject rather too narrowly, failing to realize that the same kind of energy and enterprise needed to extend their sales in the United States, is needed in the Philippine Islands; while they too often neglect the fact that they must do all they can to stimulate importations from the Islands in order to enlarge the buying power of the natives, and thereby improve trade with the United States. But this progress may or may not be stable in the Philippine Islands, just as in the case of other foreign countries. There is probably more reason to believe in its stablility because of the steady growth of the trade with the Philippines before the war, and because of the political relations between the United States and the Islands. Nevertheless, in this case, as in so many others, the increase in business with the United States has been partly the result of necessities growing out of the disturbance of world trade, and is not solely due to efforts on the part of manufacturers. This trade, moreover, has been carried on under extremely difficult conditions in banking. Financial relations with the

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Philippines have been rudimentary and unsatisfactory, and the Islands have had to depend very largely upon the aid of foreign banking capital.

What is going to become of our foreign trade after the war is over, not merely with the Philippine Islands, but with other countries? This is a universal subject of discussion and inquiry at the present time. Some believe the outlook will be brighter and better for our foreign business then than it is now; others seem to expect a general reaction, while still others who want to be safe, predict a period of "tapering off," during which trade will gradually decline to something like its old level. I do not belong to any of these schools of thought, but am emphatically a believer in the doctrine that the direction and amount of business after the war is over will depend very largely upon ourselves. If we want the business, we can have it; and we can have it in large measure because of the immense demand that will exist for our goods during the great period of reconstruction that will set in when the war is over. Moreover, we can, if we will, preempt many undeveloped fields of foreign business which, at the present time, are comparatively free from competition, and which, after the war, will not be exploited even to the extent they have been in the past, because exporters and manufacturers in foreign countries will be unable to regain their hold immediately, and will only after considerable time, be in position to devote

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to the cultivation of these foreign fields the same energy they gave them before the international convulsion which began in August, 1914. What is the duty of the American banking and business community in these circumstances?

I do not wish in the least to underestimate what has been done by some enterprising and able business concerns in preparing themselves for the continued development of their foreign markets. The effect of the great foreign trade that has been thrown, one might say forced, into our hands during the past two years, has been to educate many elements of our business public out of the parochial, almost insular attitude on this subject they had entertained in the past. They now recognize the importance of foreign business as a balance wheel and regulator of all business, as a diversifier of production, as a means of equalizing and stabilizing prices, and last, but not least, as a source of valuable additional profit, irrespective of the strength of home demands. But it must also be admitted that there are large sections of the business community which are indifferent to this point of view, and which are apparently simply waiting for something to turn up, leaving it to Providence or some political party to take care of their future business abroad, trusting that when the war is over business may continue pretty good for a time at least, or, as Mr. Kipling has expressed it, "waiting some easy wonder, hoping some saving sign." For these, should they continue their present

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attitude, there is but little prospect of success, and they must expect to see their unwonted and unexpected business disappear in some cases almost as quickly as it came to them, unless there is definite and farseeing action on their part. There are many lines of work in the way of the development of commercial preparedness, and which must be undertaken in the near future; but of all these there is but one that is germane to the purpose of this meeting - the development of a better control of international banking by our own bankers and financiers. It is this matter on which I wish to speak to you seriously.

For many years past there has been an almost unlimited amount of talk about foreign banking, and yet the number of banking enterprises actually established abroad by American bankers prior to the passage of the Federal Reserve Act, could be counted on the fingers of one hand. The Federal Reserve Act, as you know, provides for the establishment of branch banks, by properly qualified institutions, in foreign countries, and it also authorizes the Federal reserve banks to establish agencies in such countries. Only two national banks, so far as I am aware, have taken advantage of this permission, and of these but one, an eminent and ably managed institution of great resources and far-reaching vision, has entered the field on a large scale. A few months ago there was an outcry among business men's associations for an amendment to the Federal Reserve Act that would permit bankers to join together for

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the purpose of organizing such branch institutions. The demand was heeded, and on September 7, 1916, Congress, at the request of the Federal Reserve Board, so amended the Federal Reserve Act as to permit such jointly owned banks to be organized. Thus far no such banks have been established, and I am not aware of any proposals to create them that are likely to come to a head in the near future. Perhaps there are some of which I am not aware, but certainly the movement has not gone far, if indeed it has ever been started. We must conclude, therefore, that the banks of the country have not gone actively into the task of preparing themselves for the struggle to retain our foreign trade after the change of conditions which all admit must come when European conditions materially alter, and when competition is restored to something like its former intensity. The Federal reserve system has made a beginning by undertaking preliminary arrangements looking to the designation of foreign agencies intended to assist in fulfilling the purposes of the system in so far as these relate to foreign operations. I need not, however, insist upon the fact that the Federal reserve system has a purpose which is essentially different from that of ordinary commercial banks, and that whatever it may do in promoting our relations with foreign countries and in aiding in the general plan to promote the welfare of the American discount market, it can not perform the task which only strong commercially organized institutions can fulfill - that of exploiting

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and developing the foreign market in the interest of our own business community.

It is to be feared that some of our bankers look at this question as if it were a question of immediate profit solely. They are inclined to inquire into the possible profits to be gained by the establishment of branches and connections abroad, as if it affected only them and the welfare of their institutions. The question is, however, a good deal broader than this, since, as I have just shown, it involves the whole matter of retaining our trade and developing it in markets other than our own domestic fields. The business man will not be able under existing conditions in trade and industry, to carry on the campaign alone. He must have that powerful assistance which only the banker can afford, and this can not be rendered without special organization and cooperation for foreign trade in the way that I have spoken of. There are two methods by which such effective cooperation can be accomplished; one, the actual establishment of branches abroad, the other the establishment of connections with some institution which will faithfully and earnestly represent the interests of our own bankers and business men in those foreign countries. And just here let me speak to you briefly of the Philippine National Bank in its relation to American trade and business.

I have already explained that our trade development in the Philippine Islands thus far has been partly the result of fortuitous conditions, and partly the result of a gradual comprehension of the needs and characteristics of Oriental buyers. I have also briefly suggested

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that this development has occurred under very difficult banking conditions. In China and Japan there are a number of notable financial institutions of large capitalization, sound management and broad connections. Some of these institutions have branches in Manila, and in the past have done a large part of the banking business there. There has been no particular reason why they should seek to develop the resources of the Philippines, and they have very naturally confined themselves quite generally to exchange operations and a limited class of commercial business in the Islands. The Philippine Government has been obliged at times to supplement local banking activities by making advances, sometimes through local banks, to agricultural and other enterprises in the Philippines. As is well known, it has also exercised through its Treasury Department the function of maintaining the currency of the country at a parity with gold. It has been felt for a good while that something more was needed, and this without in the slightest degree reflecting upon the service already rendered by bankers or outside institutions which have established themselves in the Philippines, or by the efforts of such local capital as is invested in the banking business there. The purpose to be accomplished was that of furthering and developing local business, of connceting it with the trade and banking organizations of the United States, and of insuring after the termination of the present special and peculiar conditions, a continuance and improvement of the trade progress characteristic of the recent past.

The Philippine National Bank is thus a natural outgrowth of conditions, and affords a suggestion of one way in which distinct

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and organized effort must be made looking to the retention and improvement of foreign trade. The Bank has taken over most of the banking functions heretofore exercised by the Government, and is supplementing existing banking institutions by undertaking operations which they have not cared to go into, or else were not fitted to take up. It is to some extent unavoidably occupying the same field as these other institutions, but it in no wise seeks to limit their business, but rather to further it. Since its organization it has stood ready at all times to rediscount any paper that might be presented to it locally. As time goes on, it may be expected to establish branches elsewhere in the Orient, and particularly in the Philippines, and thus to become a general Oriental institution, not c confining itself exclusively to the Philippines, but endeavoring to develop trade between the Philippines and other parts of the East. For the present its work is naturally confined to the Islands themselves. It has already established twenty-seven agencies in as many provincial capitals, where deposits are received and exchange sold, and at which applications for loans may be filed for transmission to Manila. A regularly organized branch at Iloilo has been opened, and a branch fully equipped for business is shortly to be in operation in New York. The Bank has established relations with correspondents in Japan and on the China Coast, and is selling and buying exchange upon Eastern points generally.

The interest of American business men in the new institution should be genuine if they are at all concerned in Eastern trade. Inasmuch as the Philippine National Bank is endeavoring to do a substantial local

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business, discounting paper and assisting the development of Philippine enterprises, it is in a position to help in the expansion of insular business to a very material extent. One of the objects of its creation has been that of carrying further and rendering more effective the work of the former Agricultural Bank which had already rendered good service in helping the growers of sugar, hemp, tobacco, and other agricultural products. At the opening of the Bank's business, it, of course, undertook the duty of making agricultural loans. These are carefully limited by law to one-half of its capital and surplus, plus such sums as may be received through the sale of agricultural bonds based on its mortgage loans. The new Bank has carried thus during the present season, large loans to sugar growers, and has made considerable advances in connection with the milling of sugar. American business men who are looking to the development of a market in the Philippine Islands are being accommodated through the usual methods of opening credits and financing importations; while, as already seen, local exporters are being aided in bringing their products to market, as well as in merely aiding the shipment of them abroad. The Bank has opened credits in the United States for some of the principal importers in the Philippine Islands, and has also begun financing operations between Manila and the adjacent coast of China. In all this the new Bank will be an important factor in stimulating and developing our trade with the Philippines.

The Bank had an authorized capital of 20,000,000 pesos, or $10,000,000 gold, of which 10,100,000 pesos has been subscribed by the Government of the Philippine

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Islands. The remainder of the stock is offered to public subscription, and is being gradually sold and taken up. As the depositing of insular, provincial and municipal funds throughout the Islands with the bank is made mandatory, except in cases where public well-being may demand the use of other banks, the institution already has control of a large volume of public funds. Its resources approximate 66,000,000 pesos, or about $33,000,000 in American currency.

The president and vice president are appointed by the Governor of the Philippine Islands; and since the Government controls a majority of shares, it will always control a majority of the board of directors. The transaction of general Government business, the receipt of current deposits, payment of Government checks, making of remittances to foreign countries, and the like, are now in the hands of the Philippine National Bank, so that its duties are distinctly of a public character from many standpoints.

Perhaps there are some of you who are inclined to suggest that the organization of the Philippine National Bank transgresses views which you have formed about the interference of the Government with private enterprise in banking. And yet, in one aspect the idea of the Philippine National Bank in that regard is very similar to the basic conception of the Federal reserve system. It is not based upon the idea of Government interference with banking, but rather of Government cooperation with the community in rendering banking more effective. The Federal Reserve Act was framed upon the

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theory that by the use of the banking energy of the country in a combined and united form, supported and sustained by the power of the Government, great benefit could be rendered to every element in the community, both agricultural, commercial and industrial. The conception upon which the Philippine National Bank is founded is the same, and the ideas underlying it are identical with those underlying the Federal Reserve Act. It proceeds upon the theory that public oversight and public management in banking are desirable, that the public is entitled to realize legitimate profits upon the funds which it places in a bank, and that private initiative and private management in the operation of banking concerns are likely to be more successful and efficient than the work of public officers, however faithful and devoted these may be. The Philippine National Bank, established under different auspices and meeting very different local conditions, is thus a special application of the conception of the Federal Reserve Act to the business affairs of a far distant people whose development is at present much behind that of the United States. That the bank has justified itself may be more fully understood when I speak of its growth in resources from about 9,000,000 pesos early in May last, to about 66,000,000 at the close of the year. A part of this growth is, of course, due to the gradual taking over of public deposits and public business, but a very large part of it is due also to the increasing confidence of the business community in the institution, and to the rapid growth of the deposit and loan ac-

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counts of the business public which had dealings with it. The Philippine National Bank is doing its part to attain the end which might from another angle have been approached by our own banks had they chosen to undertake the establishment of banking organizations in the Philippines for the purpose of obtaining and definitely holding the trade of the Islands, or encouraging the improvement of agricultural and productive conditions, and of assisting in the advancement of manufacturing enterprises there.

Doubtless it would not be feasible for American institutions to go so far in the devotion of resources to the development of business in foreign countries as they would be justified in doing in the Philippines, or as the Philippine National Bank is undertaking to do. And yet the experience of this bank is in line with that of banking institutions organized by foreign countries for the purpose of operating abroad and points out the only true way in which to foster and retain foreign trade. This is through the extension of accommodation under wise and conservative conditions, to those business interests in other countries which require that kind of assistance, and which in return for it, or as a condition of getting it, will be willing and ready to turn their purchasing power toward the United States. We have long known that England's powerful hold upon the trade of South America and the Far East was not due to any innate fondness on the part of the people of

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those regions for Great Britain or her assistance, but was due to the fact that British banking institutions stood ready to facilitate the movement of goods to those countries, while they also stood stood ready within reasonable limits to assist in the development of the resources of those countries, and in the exportation of their products to Great Britain. The progress which has been made in recent years by German bankers and business men in competing with Great Britain and her representatives, has been due to Germany's recognition of the essential basis for British trade, and her adoption of similar modes of getting and controlling business. The real question in the whole matter is: Do we want to continue our present control of foreign trade, or are we content to return to the foreign trade situation which existed before the European war? If we do in fact believe that benefit comes to the country from the maintenance of a strong and well-diversified foreign trade, it will be necessary for us as a nation to adopt those measures and methods which experience has shown to be requisite.

As I have already intimated, I do not believe strongly in the effect of artificial legislation in sustaining and extending our business. In order to deal with foreign countries successfully we must not only sell but buy. We must do more than this. We must hold out the help necessary to enable our own business men to place their goods on foreign markets with success and at reasonable cost, and we must enable shippers in this country to export without unreasonable sacrifice. Indeed we must, if we wish to create a permanent and

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growing foreign trade, aid producers and shippers abroad by every legitimate means in our power, to increase their output, and to market it under favorable conditions. The idea that this can not be done, or that some special difficulties stand in the way, or that the problem is being prematurely presented, or that for some reason we can escape immediate action upon it, has been dispelled by the events of the past two years. It must be evident to all that the present moment is one which calls for the exercise of constructive business ability and the display of enterprise and initiative by our people along every line that experience shows to be required in facilitating the growth of business. Our relations with the Philippines afford merely an intimation of what can be and is being done in turning trade toward the United States, in financing it, in economizing the expenses necessarily incurred in connection with it, and generally in bringing the foreign producer and buyer closer to the home producer and buyer.

What I have said thus far has been expressed in purely general terms; and I am unwilling to leave the subject this evening without placing before you a definite problem.

First of all, I believe it to be necessary that our bankers should to a much greater extent that at present, make actual, practical connections abroad. This should be done either through the establishment of branches of their own at strategic points, or through the perfecting of agency relations with other

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banks which can be relied upon to promote the interests of the United States and its business men. In a considerable number of instances the foreign connections I speak of must be effected by the actual and direct establishment of branches, rather than through the agency method.

Secondly, our bankers generally must endeavor, so far as they can, to promote the progress and aid in the development of the foreign business of banks chartered under American control, and directly concerned to promote American interests. Our business men must cooperate in this regard by placing their business wherever possible with such banks. This is not a counsel of opposition or hostility to any foreign banking institution; it is merely a suggestion that so far as practicable, we unite as a business community in forwarding by all legitimate means our own interests abroad.

Third, the Federal reserve system should, and will, as conditions permit, establish abroad agency connections which will enable the Federal reserve banks to assist in the foreign operation of such other banks as are formed to promote trade in other countries, and will at the same time undertake those operations designed to maintain the stability of monetary and exchange relationships between ourselves and other countries which are called for by the Government banks elsewhere.

Fourthly, our business public must undertake to furnish a direct, practical support to these efforts on the part of our banks; looking at the matter from the long range standpoint, and recognizing that while they may have to submit to

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some difficulties or even inconvenience while we are extending our banking relationships abroad, these are incurred merely for the sake of developing a system which in its turn will safeguard the interests of the business public when the intensity of competition is restored, and when the effort of European countries to obtain a share of foreign markets again becomes active.

This is a large program, but the same may be said of everything that is destined to exert a far-reaching and permanent effect. A great deal of such success as may be attained will be secured through the active interest and enterprise of the younger bankers of the country; upon them will fall the actual work of undertaking the tasks involved in the extension of our banking connections, and to them undoubtedly will be assigned most of the constructive duties involved in the investigation and analysis of foreign conditions. New conditions must be met, and old ones must be adapted to them. The work is one which calls for vision and imagination, as well as for the technical knowledge of experienced men who have a definite purpose to accomplish, and who are able to separate what is possible from what is visionary and unattainable. This is why I have brought the subject to your attention as one who has had a small share in the working out of one phase of the problem, who sees the field that is open, and who recognizes that although the harvest is ripe, the reapers are very few indeed. If I have at all contributed to making our foreign problem more vivid in your minds and in persuading you to a more pointed recognition of the need for immediate action I shall feel that a further step has been taken towards its definite solution.

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CHAIRMAN
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COMPTROLLER OF THE CURRENCY

FEDERAL RESERVE BOARD

WASHINGTON

977

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

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

January 15, 1917.

Gentlemen:

In accordance with arrangements already made the Federal Reserve Board will publish a supplement to the par list as of February 1, 1917.

Will you please, therefore, forward such changes as should be made for your District to reach Washington not later than January 23d?

Very truly yours,

Secretary.

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1917

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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

January 17, 1917.

Dear Sir:

In answer to inquiries received from some banks as to proper methods of classifying the discount material on hand under the several heads shown in the lower portion of Form 38, especially under the head of "Agricultural and live-stock paper", I would say that it is the desire of the Board that the Federal reserve banks ascertain in all cases whether the original loan has been obtained from the rediscounting member bank for agricultural, industrial or commercial purposes so that all discount items of the Reserve Bank might be reported to the Board properly classified.

In classifying the discount material the reserve banks should in the first place be guided by the stated purpose of the original loan, as reported by the rediscounting member bank. In case this purpose is stated only in general terms, as e. g. "in accordance with Section 13", the occupation of the borrower should be used as a guide in classification. Thus, if John Smith, a merchant, who is also engaged in farming, gives an unsecured note to Henry Jones, engaged in the fertilizer business, it would seem entirely proper to report the item as "Unsecured commercial and industrial paper", unless there is information on hand which makes

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it clear that Jones was to use the proceeds of the loan for agricultural purposes. In case the note was secured by twenty bales of cotton, it would be proper to report it as "commercial and industrial paper - secured", unless the purpose of the loan was clearly stated to be agricultural. Nor would it make any difference in classification were the payee of the note reported as "farmer".

In case Farmer Smith gives to Richard Jones a note secured by a lien on 25 steers (documents attached to note or not) it would be proper to report the item as live-stock paper, unless there is information to the effect that the proceeds of the loan have been or are to be used for agricultural purposes.

It is clear that all six-month paper is to be reported either as agricultural or live-stock paper. Item "Total bills discounted", shown in the lower half of Form 38, should, of course, equal total of subdivision 1, - (Bills discounted - Members), in the upper half of the form.

It is realized that the above explanations by no means exhaust all possible combinations, but it is thought that they will prove helpful to your discount department in the preparation of the weekly statement on Form 38.

Very truly yours,

Vice Governor.

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AND FISCAL AGENT
ADDRESS REPLY TO
FEDERAL RESERVE BOARD

January 19, 1917.

Dear Sir:

In view of the fact that the rate for bankers' acceptances recently maintained by Federal reserve banks has been somewhat higher than the open market rate, the holdings of acceptances by the Federal reserve banks have been materially reduced during the past weeks.

In consequence the Board has received letters from some of the Federal reserve banks expressing apprehension that their earning assets might be reduced too drastically, and some of the banks have shown some inclination to invest in warrants, even at low rates, and for the full period permitted by law.

The Board therefore has thought it advisable to direct me to address a letter to all Federal reserve agents in order to secure a better understanding of the policy which in its opinion, should be pursued at this time.

During the month of December, and up to January 12, the net gold imports into the United States amounted to about $169,000,000. Excess reserves have materially increased in consequence. It may be assumed that this plethora of gold is not entirely a natural one and that much of it will be absorbed by impending flotations of new securities, after which we shall probably witness again the same development that has been characteristic of similar periods in the past - that the deposit and loan structure will again expand so as to absorb large portions of the new gold.

There is general agreement that this continuous and rapid growth of deposits and loans is not without danger. With the present ease of money, it would appear, therefore, in the opinion of the Board, to be a wise policy to permit the earning assets of the Federal reserve banks - which combined amount to about $206,000,000 - to be reduced by from forty to fifty millions,

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and thereby to absorb, temporarily at least, an equivalent amount of the newly imported gold. Of course, such a policy must be carried out in a careful and tactful way, and no definite amount can be fixed at this time to which the investments of the Federal reserve banks should be reduced. Changes in conditions may occur at any moment, which may render it necessary to reverse this policy, or to apply it even more radically than is now contemplated. During the past few weeks Federal reserve banks have operated along these lines with very good results, and acceptances and rediscounts have been reduced by about $40,000,000 since they reached their highest point, early in December. So long as the present ease continues, there should not be any difficulty in continuing the present policy. By permitting the open market to absorb the bankers' acceptances, the additional object is gained of training the member banks to deal in acceptances and to become accustomed to investing in them.

In expressing to you these thoughts the Board wishes me to add that it hopes that the banks will not become unduly restive because of a temporary reduction of their earning assets. The Board has no doubt that before the year just begun is past, many occasions will arise which will enable the Federal reservebanks to employ their funds actively, but the Board considers it the primary duty of the Federal reserve banks to be mindful of their obligation to do their full part in preventing just now a rapid expansion of credit and in accumulating resources to be used when active demands are made upon them for ordinary commercial credit facilities.

Very truly yours,

Governor.

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FORM OF RESOLUTION AUTHORIZING A FEDERAL RESERVE BANK TO SHIP UNFIT FEDERAL RESERVE NOTES OF ANOTHER FEDERAL RESERVE BANK DIRECT TO THE TREASURER OF THE UNITED STATES FOR REDEMPTION.

At a meeting of the Board of Directors of the Federal Reserve Bank of _____, called pursuant to the provisions of the by-laws of said bank and held on the _____ day of _____, 191 , the following resolution was offered, seconded and duly adopted:

"BE IT RESOLVED, That the Federal Reserve Bank of _____ be and hereby is authorized, empowered, and directed to forward to the Treasurer of the United States for redemption for and in behalf of this bank all unfit Federal reserve notes issued by this bank which the Federal Reserve Bank of _____ may now or hereafter hold, and to do and to perform every lawful act necessary to effect such redemption in the manner outlined in the circular letter of the Federal Reserve Board, dated January 15, 1917, relating to unfit Federal reserve notes forwarded to the Treasurer of the United States for redemption by a Federal reserve bank other than the Federal reserve bank of issue."

I hereby certify that the foregoing is a true and correct copy of a resolution adopted and spread upon the minutes of the Board of Directors of this Bank, held on the date specified.

_____
Cashier or Secretary,
Federal Reserve Bank of _____

1/22/17.

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1952

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
985 FEDERAL RESERVE BOARD

January 23, 1917.

Dear Sir:

The Board has been requested by several of the Federal reserve banks to prepare a form of power of attorney to be used in connection with the plan set forth in its letter of January 15, 1917, whereby unfit Federal reserve notes may be forwarded to the Treasurer of the United States for redemption by Federal reserve banks other than the bank of issue.

Inclosed herewith is a form of resolution which is submitted merely as a suggestion and which may be altered in any manner the Federal reserve banks may deem advisable.

It is requested, however, that you send to the Treasurer of the United States copies of whatever resolution you may adopt authorizing any Federal reserve bank to act as your agent in forwarding Federal reserve notes to Washington for redemption.

Respectfully,

Governor.

Inclosure.

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1953

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FEDERAL RESERVE BOARD

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SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

988 ADDRESS REPLY TO
FEDERAL RESERVE BOARD

January 23, 1917.

Dear Sir:

A number of letters have been addressed to the Federal Reserve Board, raising the question whether a trade acceptance, which is defined in the Board's regulations as "a draft or bill of exchange drawn by the seller on the purchaser of goods sold and accepted by such purchaser," includes a draft or bill of exchange based on the purchase of advertising space.

The term "goods" as used in the regulations of the Board includes wares, merchandise, or agricultural products including live stock, and because of the doubts raised as to whether this term is broad enough to include advertising space, the Board has ruled that a draft or bill of exchange drawn by a publisher, or other advertising agency, on the purchaser of advertising space and accepted by such purchaser shall be considered a trade acceptance, provided the advertisement on which the draft or bill is based is for the purpose of promoting or facilitating the production, manufacture, distribution, or sale of goods, wares, merchandise, or agricultural products, including live stock; and provided, further, that such advertisement is not illegal, and is not for the purpose of promoting or facilitating any transaction which is prohibited by the laws of the State in which it is to be consummated.

Each Federal reserve bank should take such steps as it deems necessary to satisfy itself that a trade acceptance covering the sale of advertising space is of the character described in this letter.

Respectfully,

Governor.

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Federal Reserve Bank of St. Louis

1954

989
(revised)

Division of Audit
and Examination.

FEDERAL RESERVE BOARD

Washington.

MEMORANDUM FOR THE AUDITOR:

Kindly furnish to the Federal Reserve Examiner, examining your bank as of close of business _____, the following:

1. Statements of account current to be sent to all member banks as of close of business_____.

2. Statements to be sent to other Federal reserve banks.

3. Immediately upon receipt of daily statements from other Federal reserve banks as of close of business _____, reconcile, and turn over to Examiner copies of such reconcilements to be retained by him.

4. Daily statement, Form 34, 3 copies certified to by cashier.

5. Report of earnings and expenses, to be brought up to date, Forms 95 & 96.

6. Expenses of Transit Department brought up to date, Form 97.

7. Estimate of accruals:
   (a) Loans and discounts
   (b) Acceptances (open market purchases)
   (c) Warrants
   (d) United States Securities
   (e) _____
   (f) _____

   Transit service charges collectible

   Less amount payable to other F. R. Banks.

8. Estimate expenses unpaid:
   (a) Salaries
   (b) Rent
   (c) Directors fees
   (d) Sundry

9. Proof of expenses paid in advance and other deferred accounts.

10. Changes in furniture and equipment account.

11. Changes in cost of Federal reserve notes since last examination.

12. Inventory of machines and mechanical devices, giving kind, number, etc.
    Transit machines, Burroughs
    Adding machines, "
    Typewriters, Underwood.

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Federal Reserve Bank of St. Louis

1955

990
(revised)

Division of Audit
and Examination.

FEDERAL RESERVE BOARD

Washington

MEMORANDUM FOR THE CASHIER:

Kindly furnish the information requested below for the use of the Federal Reserve Examiner, examining your bank as of close of business _____.

1. List of officers and employes, by departments (Form is attached, and paper and carbon will be furnished).

2. Three copies of each circular or regulation issued by the bank since the last examination.

3. Custody of cash: If there is any change since last examination, please give detailed memorandum of where kept, under whose control, protection, etc.

4. List of insurance and fidelity bonds carried - fidelity, burglary, registered mail, fire, etc. - showing expiration and premium paid.

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Federal Reserve Bank of St. Louis

1956

Division of Audit
and Examination.

991
(revised)

FEDERAL RESERVE BOARD

Washington

MEMORANDUM FOR MANAGER OF TRANSIT DEPARTMENT:

Kindly furnish the information requested below for the use of the Federal Reserve Examiner, examining your bank as of close of business _____.

1. Number of member banks:
   National _____
   State _____

2. Number of non-member banks in district.

3. Number of non-member banks upon which items are collected.
   Through member banks _____
   Direct _____
   Through other non-members _____

4. What items are received for immediate availability?

5. Form of settlement accepted from non-members.

6. Daily averages of items handled, for three months period preceding, by calendar month (either first to first or 16th one month to 15th of next), in following form:

Period covered	Your city	Elsewhere within district	Other F.R.Dist	Total Number

Amount (even thousands)

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7. Expenses of Transit Department, such as salaries, rent, telephone and telegraph, postage, expressage, printing and stationery, insurance and fidelity bonds, depreciation, etc., for current or previous month.

8. Service charges collected over same period.

9. Service charges collectible for same period.

10. Service charges (per item charged)
    (a) To member banks
    (b) To Federal reserve banks

11. Service charges paid to other Federal reserve banks.

12. Service charges collected since inauguration of system in July 1916; actual to last day of previous month and estimated to date of examination, showing from what sources derived, as follows:
    Reserve city banks
    Other member banks
    Federal Reserve Banks

    Service charges paid to other Federal reserve banks since inauguration of system in July 1916; actual to last day of previous month and estimated to date of examination.

    Total cost of transit department; actual expenses to last day of previous month and estimated expenses since.

13. Deficient reserves - how covered?
    How have penalties been assessed?
    How often is report of net deposit balances called for?
    (a) Reserve city banks
    (b) Other member banks

14. Three copies of any changes in the Clearing House rules since the inauguration of the collection system in July 1916.

15. Operationsin purchase and sale of bank transfer; schedule of rates, earnings by months.

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Federal Reserve Bank of St. Louis

1958

EX-OFFICIO MEMBERS
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H. PARKER WILLIS, SECRETARY
SHERMAN P. ALLEN, ASST. SECRETARY
AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD
994

January 26, 1917.

Dear Sir:

On behalf of the Committee on Clearing of the Federal Reserve Board I beg to state that it is the belief of the Committee that it is important that we should make ready and have our plans formulated as to the next step that should be taken in advancing the operations of the clearing and collection system. Congress will adjourn on March 4th and we will then know what, if any, steps have been taken in respect to the Kitchin amendment. At the present time it does not look as if there were much likelihood of the Kitchin amendment being adopted. If it is not, it will become the duty of the Board and the Federal reserve banks to go ahead energetically and perfect the system, the most serious objection to which at the present time is the fact that there are still some 7,000 banks who do not remit at par. In laying our plans for the future I desire to ask for comments from you upon the following suggestions and statements:

(1) It would appear that one of the greatest obstacles to progress is the attitude of many of the local clearing houses; for instance, we have a recent case where under the clearing house rules of Macon, Georgia, the banks impose a charge of one-eighth of one per cent for a check which would be given immediate credit at par at Atlanta, only eighty-eight miles away; whereas they accept at par checks drawn on Philadelphia or New York. How shall we meet this situation, and has the time come for the Board to promulgate rules, as contemplated in Section 16, which will specify the maximum charges which a member bank may make against its customers?

(2) As indicating the sort of adjustment which should be made with clearing houses if they are willing to meet the views of the Federal Reserve Board and the Federal reserve banks, I would point out that in quite a number of important clearing houses a differential <u>in favor</u> of checks of banks that can be collected through the Federal reserve bank at par is made, as compared with checks which cannot be so collected. Such a differential operates to assist the Federal reserve bank in extending its par list. In quite a number of cases, however, all checks of certain areas are taken on the same

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basis regardless of how collected. This means that the checks collectable through the Federal reserve bank have no advantage over those not so colletable. This method, while not ideal, is, obviously, more advantageous to the Federal reserve bank than that described in No. 1, where checks collectable through the Federal reserve bank are actually discriminated against.

(3) We are getting ready to offer country banks the privilege of issuing drafts against Federal reserve banks, which will be given immediate credit and availability not only at the bank upon which drawn, but at one other designated Federal reserve bank. This will be a privilege of considerable value to member banks, but it is assumed that it will be accompanied, or followed soon after, by the granting of the privilege of collecting for country banks time items, on terms at least as favorable as the terms heretofore afforded by city banks to their country correspondents.

(4) The officers of several of the Federal reserve banks have expressed themselves as believing that not much more progress can be made in enlarging the volume of transactions offered for clearing and collection until Federal reserve banks express themselves as willing to collect items on nonassenting State banks and trust companies. In a number of the Districts arrangements are being perfected for the collection of items of this character through express companies, but in some Districts it is impossible to reach all of the banks, even through express companies, and it may in those cases be necessary to adopt the Post Office method. Collection through express companies will, however, enable the collection of a great many nonassenting member bank items and it would appear as though in the more thickly settled Districts, such as New York, Pennsylvania, and Cleveland this matter should be immediately taken in hand.

(5) At the last meeting of Governors a plan was submitted by the writer under which a scale of charges as between Federal reserve banks and member banks, and as between member banks and their customers was proposed. It was the opinion of the Governors that the time was not opportune for putting out this schedule of charges; also that the rates suggested were too high. Is this still your view, and if you believe that the scale of charges is too high, have you any counter suggestions to make?

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(6) To what extent can the clearing system be made more popular with bankers in reserve cities - or in other large cities with similar banking facilities - by the adoption of a plan similar to that adopted in Dallas and about to be adopted in the Kansas City district? This plan provides for the direct interchange of items between cities, and drawing on the Federal reserve bank for items sent direct. This plan has the merit of cutting down float, of relieving the Federal reserve bank of cost of handling a good many items, and, lastly, of putting the banks in cities thus inter-connected on a parity.

Yours very truly,

Chairman,
Committee on Clearing.

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P R E S S S T A T E M E N T.

January 29, 1917.

The Federal Reserve Board to-day made public the text of a memorandum transmitted to it by Mr. James B. Forgan, President of the Federal Advisory Council, expressing the views of that body with reference to the proposed amendments to the Federal Reserve Act recently submitted to the Banking and Currency Committees of the two Houses of Congress by the Federal Reserve Board.

It will be noted that the Council unanimously approved the proposed note issue amendment which has been stricken out by the House Committee on Banking and Currency, and that the Council has suggested a modification of the proposed reserves to be carried by member banks with the Federal reserve banks. In view of the fact, however, that the House Committee struck out all requirements for vault cash, the Board believes that the suggested reserves of seven, ten, and thirteen per cent respectively for country banks, reserve city banks and central reserve city banks, should be retained.

The Advisory Council's memorandum, dated January 25th, is as follows:

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RECOMMENDATIONS BY
THE FEDERAL ADVISORY COUNCIL IN REGARD TO THE AMENDMENTS
TO THE FEDERAL RESERVE ACT PROPOSED BY
THE FEDERAL RESERVE BOARD

JANUARY 1917.

No. 1. AMENDMENT TO SECTION 16 which provides

(a) for the issue of Federal reserve notes directly against the deposit of 100% gold; or 100% of paper, or both;

(b) for the counting of gold held by the Federal reserve agents as security for notes, as part of the gold reserve required to be held by the bank against such Federal reserve notes;

Meets with the approval of the Federal Advisory Council.

No. 2. IN RE. AMENDMENT OF SECTION 19, abbreviating and simplifying the clauses in Section 19 which relate to reserve requirements. This provides that all member banks shall maintain reserves in the Federal reserve bank as follows:

	Against Demand Deposits	Against Time Deposits
(a) Country banks	7%	3%
(b) Reserve city banks	10%	3%
(c) Central Reserve city banks	13%	3%

and in addition every member bank is required to keep in its own vault for till money an amount of specie or currency (not necessarily gold or lawful money) equal to five per cent of its demand deposits, less the amount of net balance with Federal reserve banks in excess of the minimum above stipulated.

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This amendment is in harmony with one of the basic principles of the Federal Reserve Act to the effect that the bulk of the gold held as reserves for bank deposits should be mobilized in the Federal reserve banks. From the standpoint however of a practical working basis the Council doubts if so much as is proposed of the member banks' available cash should be arbitrarily tied up in the form of compulsory balances with the Federal reserve banks.

The Council at its meeting of September 19th last, drew the Board's attention to the fact that until the State banks join the system and daily clearing house balances can be settled by checks on the Federal reserve banks the member banks, especially in the large cities, must keep a sufficient supply of gold or lawful money on hand for the settlement of such balances as well as for their counter use. Besides this it would be a conservative policy for the member banks to keep in their own vaults a reasonable amount of gold or lawful money proportionate to their demand deposits. Banks located in Federal reserve cities now receive from the Federal reserve banks late in the afternoon checks on themselves in large volume and amount which have accumulated during the day and have been charged against their legal reserve balances in such large volume and amount as to hamper them in maintaining their legal reserve balances. In our opinion 5% cash on hand would not be sufficient for these purposes and from a practical standpoint it would facilitate the oper-

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ations of the member banks if the minimum compulsory balances to be kept by them with the Federal reserve banks against their demand deposits were at least reduced 1% in each class and the percentage of the till money correspondingly increased in the case of the reserve city and central reserve city banks, the increase in till money in the case of the country banks being unnecessary. The Council's recommendation is therefore as follows:

	Deposits in Federal Res. Banks against Demand Deposits.	Deposits in Federal Res. Banks against Time Deposits.	Till Money
Country Banks	6%	3%	5%
Reserve City Banks	9%	3%	6%
Central Reserve City Banks	12%	3%	6%

No. 3. 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.

The Council is of opinion that it would be undesirable and unnecessary to grant such power to the Federal Reserve Board. The Board would only take action under such power when member banks are overburdened with surplus cash reserves and its action then could only apply to member banks. The effect would therefore be that member banks would be compelled to increase their noninterest-bearing balances with the Federal reserve banks while

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nonmember banks would have the free use of their funds. It would place another stumbling block in the way of State banks joining the system.

No. 4. AMENDMENT OF SECTION 13, 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 Feferal reserve bank in an amount to be determined under rules prescribed by the Federal Reserve Board.

This might work to the mutual advantage of the member banks in connection with the check collection system and of nonmember banks willing to conform to the rules prescribed by the Federal Reserve Board as well as to that of the Federal reserve banks through the compensating balances. The experiment might be worth trying.

No. 5. 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 services is not incumbent upon them in their capacity as directors.

The Council would recommend that the proposed addition to Section 22 commencing with "PROVIDED, HOWEVER, THAT NOTHING IN THIS ACT CONTAINED" should be amended as follows:

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PROVIDED, HOWEVER, THAT NOTHING IN THIS ACT CONTAINED SHALL BE CONSTRUED TO PROHIBIT A DIRECTOR, OFFICER, OR EMPLOYEE FROM RECEIVING THE SAME RATE OF INTEREST PAID TO OTHER DEPOSITORS FOR SIMILAR DEPOSITS MADE WITH SUCH BANK: OR TO PROHIBIT A DIRECTOR, WHO IS NOT AN OFFICER OR EMPLOYEE FROM RECEIVING, DIRECTLY OR INDIRECTLY, THE USUAL AND CUSTOMARY COMMISSIONS OR FEES FOR SERVICES RENDERED IN BUYING AND SELLING SECURITIES OR OTHER INVESTMENTS FOR OR ON ACCOUNT OF SUCH BANK, ~~BUT IN THIS LATTER CASE THE ACTION OF THE BOARD OF DIRECTORS, IN DIRECTING EACH PURCHASER OR SALE OF SUCH SECURITIES OR OTHER INVESTMENTS, MUST BE BY AN AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD EXCLUSIVE OF THE DIRECTOR INTERESTED. AND~~ BUT EACH SUCH TRANSACTION MUST BE RECORDED IN THE MINUTES OF THE MEETING OF SAID BOARD, SUCH MINUTES TO SPECIFY THE NAME OF THE DIRECTOR AND THE FIRM OR CORPORATION WITH WHICH HE IS CONNECTED, IF ANY, THROUGH WHICH SUCH ORDER IS ~~TO BE~~ EXECUTED TOGETHER WITH THE AMOUNT OF THE FEE OR COMMISSION ~~TO BE~~ PAID ON EACH TRANSACTION; AND, PROVIDED FURTHER, THAT NOTES, DRAFTS, BILLS OF EXCHANGE, OR OTHER EVIDENCES OF DEBT EXECUTED OR INDORSED BY DIRECTORS OF A MEMBER BANK MAY BE DISCOUNTED WITH SUCH MEMBER BANK ON THE SAME TERMS AND CONDITIONS AS OTHER NOTES, DRAFTS, BILLS OF EXCHANGE, OR EVIDENCES OF DEBT ~~UPON THE AFFIRMATIVE VOTE OR WRITTEN ASSENT OF AT LEAST THREE-FOURTHS OF THE MEMBERS OF THE BOARD OF DIRECTORS OF SUCH MEMBER BANK.~~

The Council makes this recommendation because in its judgment an affirmative vote or written assent of at least three-fourths of the members of the Board is an unnecessary restriction in connection with such services by a director as the buying and selling of securities and inasmuch as notes, drafts, bills of exchange or other evidences of debt executed or indorsed by bank directors are as a rule the very best of their class, the placing of special restrictions on the discounting of such instruments for directors would only unnecessarily and unwarrantably impede legitimate business or force it into other banks.

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No. 6. 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 and exports.

The Council approves this amendment.

No. 7. 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.

The Council approves this amendment.

No. 8. 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.

The Council has already advised the Board that it approves the authorization of 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, but disapproves the granting of such a privilege to the banks in some States while it is withheld from banks in other States irrespective of State laws affecting State banks and trust companies in regard to the establishment of branches by them.

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No. 9. AMENDMENT OF SECTION 9, to authorize mutual savings banks not having a capital stock to become associate members of the Federal reserve system under certain prescribed conditions.

The Council approves this amendment.

No. 10. 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.

The Council would recommend that instead of amending Section 18 so as to give 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 that the law providing for the exchange of 2% gold bonds bearing the circulation privilege, but against which no circulation is outstanding, for one-year gold notes to an amount not exceeding one-half of the 2% bonds so tendered for exchange, be so amended as to do away with the one-year gold notes entirely and provide that the 2% gold bonds may be exchanged for an equal amount of thirty-year 3% gold bonds without the circulation privilege.

No. 11. 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

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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.

As member banks and others doing business with the Federal Reserve Agent and his assistant would not necessarily be charged with knowledge of the absence or disability of the Federal Reserve Agent the restricted power of his assistant to act in his name and stead only during his absence or disability should for their protection be removed by striking out the words "during his absence or disability" occurring in the last paragraph of the proposed amendment. If the assistant should act in any matter of importance during the presence or disability of the Agent to act for himself his action would be null and void. Otherwise the Council sees no objection to the amendment.

1/29/17

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64th CONGRESS,
2d Session. H. R. 20540.

IN THE HOUSE OF REPRESENTATIVES.

January 26, 1917.

Mr. Glass introduced the following bill; which was referred to the Committee on Banking and Currency and ordered to be printed.

A B I L L

To authorize national banking associations to establish branches.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Act approved December twenty-third, nineteen hundred and thirteen, known as the Federal reserve Act, be, and the same hereby is, amended by adding a new section as follows:

"Domestic Branches.

"Sec. 25a. That any member bank located in a city or incorporated town of more than one hundred thousand inhabitants and possessing a capital and surplus of $1,000,000 or more may, under such rules and regulations as the Federal Reserve Board may prescribe, establish branches, not to exceed ten in number, within the corporate limits of the city or town in which it is located: Provided, That no such branch shall be established in any State in which neither State banks nor trust companies may lawfully establish

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branches: And provided further, That the number of branches which a member bank may establish shall not exceed the number of branches which the laws of the State in which said bank is situated permit a State bank or trust company to establish within the corporate limits of said city or town."

1/30/17.

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