

FEDERAL RESERVE BOARD
WASHINGTONMemorandum:

In re - Clearing House Examinations.

In nineteen cities members of the Clearing House Association and nonmembers with clearing privileges are subject to examination by the Clearing House Examiner, usually once each year. The examination is thorough, particular attention being paid to the loans, discounts and credits of the bank. After each examination a copy of the examiners report is delivered to the bank for the information of the directors. In case an unsatisfactory condition is disclosed, the report is called to the attention of the Clearing House Committee.

Clearing House Examinations have proven very effective in the elimination of unsatisfactory assets and the correction of unsound tendencies in institutions under criticism. While no disciplinary power is vested in the Clearing House Committee, still it was in a position to recommend the discontinuance of clearing privileges which in itself would be a public notice of unsatisfactory condition.

- 2 -

In Spokane the Clearing House Examinations are now being made under the supervision of the Federal Reserve Branch, the manager being the Clearing House Examiner. In Portland, it is apparently the intention to have the examinations under the supervision of the Portland Branch of the Reserve Bank. The Clearing House Association at Seattle is desirous of having the local branch undertake the examination of Clearing House member banks in that city.

In view of the fact that Reserve Banks or Branches are located in at least two-thirds of the cities where Clearing House examinations are now conducted, and further that a majority of the Clearing House members in those cities are members of or maintain clearing balances with the Reserve Bank, it is quite likely that the question of the Reserve Bank undertaking the supervision of the Clearing House Examinations is likely to be suggested to the Board in the near future for consideration.

If the Clearing House Examinations are to be undertaken by the Reserve Banks with the approval of the Federal Reserve Board, it should be definitely understood that the responsibility for such examinations shall be vested solely in the Federal Reserve Bank and

not in the Clearing House Committee. Dual control or supervision will prove very unsatisfactory. In the appointment of examiners, while it would be well to consider the suggestions of the Clearing House Association, still the Reserve Banks, subject to the approval of the Reserve Board, should appoint the examiners and have the supervision of all examinations.

With reference to the expense of maintaining the examining department, there seems to be no reason why the present joint fee system should not be continued if agreeable to the Clearing House Banks, otherwise the cost of examination should be assessed upon the bank examined, as provided for in the Federal Reserve Act. The Reserve Bank should be free to assign men in the examining division to other duties or assign them to make examinations of institutions in other cities. Reports of examinations should be filed with the Federal Reserve Bank and if an unsatisfactory condition is disclosed, the matter should be handled by the Reserve Bank officials and not the Clearing House Committee. National Banks are now examined efficiently twice each year. If a further investigation is to be made, it should be limited to loans, credits, and investments, unless a complete examination is requested by the

bank under examination.

Unless it is possible to make an arrangement as outlined above, the Clearing House examinations should not be undertaken by the Reserve Banks. The Reserve Banks should have in its files information as to the condition of all state banks and of banks maintaining clearing accounts with it. For that reason in the event of the examinations not being undertaken by the Reserve Bank, it would be well to arrange a system of cooperation with the Clearing House Associations whereby copies of reports of examinations should be given to the Reserve Bank for its files. Under such a plan it would be possible and desirable to designate a local Clearing House Examiner to act as Special Federal Reserve Examiner in the examination of State Member Banks and State Banks maintaining clearing accounts with the Reserve Banks, so that examinations made by him might be accepted in lieu of special examinations made by examiners of the Board or of the Federal Reserve Bank. This is desirable particularly in instances where it has not been possible to make satisfactory arrangements with the State Banking Commissioners, or where the report of the Clearing House examination would be preferable to that of the State Banking Commissioner.

- 5 -

Reserve Banks should have definite data as to condition, before permitting a nonmember bank to open a clearing account for the reason that the public is likely to assume that the Reserve Bank is satisfied with financial condition of such nonmember bank.

Respectfully submitted,

(Signed) J. A. BRODERICK.

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FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

November 6, 1917.

Dear Sir:-

For some weeks past the Board has been making an analysis of the items constituting the "float" and has ascertained in the case of each Federal Reserve bank the percentage that this float bears to total earning assets and to deposits. Reference is made to the table attached hereto, from which it will be seen that these percentages are by no means uniform, but that there are wide variations. In some instances the amount of the float is entirely out of proportion to what it should be and it should be remembered that investments in float weaken the loaning power of the Federal Reserve bank because it is a nominal or unavailable asset which cannot be used as security for the issue of Federal Reserve notes. However, the present figures cannot fairly be used as a basis for definite conclusions, because of the abnormally large transfers which are now being made for government account; and normal conditions are naturally obscured or affected by the loan subscriptions now in process of settlement. But the Board proposes to continue its analysis, which will, in the course of time, show more clearly the real conditions at each bank. The attached sheet is sent you for the purpose of directing the attention of your officers and executive committee to the problems involved, and with the request that careful consideration be given to the best methods of reducing the bank's investment in float. The Board wishes to be advised at your early convenience as to the interest rates adopted by your bank in dealing with transfers, purchases of checks or bills for collection and similar items which constitute float. In the opinion of the Board this rate of interest should approximate the fifteen day interest rate, and in cases where the bank is inclined to invest too large a proportion of its funds in float, it might be even higher.

Very truly yours,

Governor.

Chairman,
Federal Reserve Bank,