X-889

March 21, 1918.

S i r :

You have requested my opinion as to whether the limitations contained in Section 13 of the Federal Reserve Act relating to charges for the collection and payment of checks can be held to apply to State banks which are neither members of the Federal reserve system nor depositors in Federal reserve banks.

As originally enacted, the first paragraph of Section 13 reads as follows:

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

In Section 16, apparently as the basis of a system of check clearing or collection, it is provided that Federal

reserve banks shall receive on deposit at par checks and drafts on member and other Federal reserve banks; and the Federal Reserve Board is authorized to fix by rule the charges to be collected by member banks from patrons whose checks are cleared through the Federal reserve bank any charge for the service of clearing or collection rendered by the Federal reserve bank.

It will be noted that under the first paragraph of Section 13 in its original form the only classes of banks which might be depositors in and thus clear through a Federal reserve bank were its member banks and other Federal reserve banks, and the only checks and drafts specified as receivable on deposit were checks and drafts drawn upon member banks or upon other Federal reserve banks.

The Acts of September 7, 1916, and June 21, 1917, so amended the first paragraph of Section 13 as to extend the clearing and collection facilities of the Federal reserve system to include checks and drafts generally, to make these facilities directly available to nonmember banks and to establish the limitations as to charges referred to in the question submitted. The paragraph as so amended reads as follows:

> Any Federal reserve bank may receive from any of its member banks, and from the United States, deposits of current funds in lawful money, national bank notes, Federal reserve notes, or checks and drafts, payable upon presentation, and also, for collection, maturing notes and bills; or, solely for purposes of exchange or of 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 sufficient to offset the items in transit held for its account by the Federal reserve bank; Provided further, That nothing in this or any other section of this Act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per $100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange

or otherwise; but no such charges shall be made against the Federal reserve banks. (Italics mine)

The limitations as to charges referred to in the question submitted are contained in the second proviso quoted above. This proviso, apparently recognizing an existing right of member and nonmember banks to make reasonable charges for the collection or payment of checks and drafts and remission therefor by exchange or otherwise, provides (1) that these charges are "to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per $100", but (2) that "no such charges shall be made against the Federal reserve banks".

Clearly these limitations apply to national banks, which are compelled to be member banks, to such State banks as become member banks by voluntarily accepting the terms and provisions of the Federal Reserve Act, and to such other State banks as do not become member banks but by becoming depositors in Federal reserve banks upon the conditions specified avail themselves directly of the facilities of the Federal reserve clearing system.

The specific question to be determined is whether these limitations apply to nonmember State banks which do not become depositors but checks upon which may pass through Federal reserve banks in process of clearing or collection.

The theory and scheme of the Federal reserve legislation seems inconsistent with the purpose on the part of Congress to subject State banks against their will to Federal control or regulation. State banks are not compelled to become members of the Federal reserve system or depositors therein. Those possessing the necessary qualifications are, however, invited to become members. They are not only free to accept or decline, but if they accept remain at liberty to withdraw from the system. (Sec.9) By Section 13 as amended, State banks not desiring to become members or too small to be

eligible for membership are likewise invited to share in the clearing and collection facilities of the system by becoming depositors in Federal reserve banks. But they may accept or reject the invitation, and if they become depositors may close their accounts at their pleasure.

It would accordingly seem that the limitations referred to ought not to be regarded as intended to be imposed upon State banks not connected with the Federal reserve system as members or depositors, against the will of such banks, unless that intention clearly appears.

The term "nonmember bank" as used in the proviso may reasonably be construed as referring to a nonmember bank that has become a depositor as authorized in the preceding provisions of the paragraph. If this term is so construed, obviously the provision requiring charges "to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per $100", will have no application to nonmember State banks which are not depositors in a Federal reserve bank. The broad language of the concluding clause, "no such charges shall be made against the Federal reserve banks", may be construed not as directed against State banks which are not depositors but merely as specifying a condition upon which checks may clear through the Federal reserve banks -- in effect a prohibition against the payment of such charges by the Federal reserve banks.

Under this construction, member banks and nonmember banks which are depositors in the Federal reserve banks will be subject to the limitations in the proviso but nonmember banks which are not depositors will not be subject to the limitations. All, however, will have to adjust their charges among themselves and with their own depositors, the Federal reserve banks being prohibited from paying such charges.

This construction seems to be in harmony with the intention of the framers of the amendment to Section 13 embodying the above mentioned proviso.

The Act of June 21, 1917, amending Section 13 and other sections of the Federal Reserve Act, as originally introduced in both the House and Senate contained no part of the (second) proviso, the section in the proposed amended form ending with the preceding proviso. The Senate, adopting an amendment offered by Senator Hardwick, added the second proviso in the following form:

> Provided further, That nothing in this or any other section of this Act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, but in no case to exceed 10 cents per $100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise. (55 Cong. Rec. 2065.)

It was thought the effect of the Hardwick amendment would be to recognize the right of any bank upon which checks are drawn to make charges against the Federal reserve bank through which such checks might be cleared or collected. The Hardwick amendment was opposed by the Federal Reserve Board, as appears from letters from its Governor to Senator Owen and Congressman Glass, Chairmen of the respective Committees on Banking and Currency of the Senate and House. (Pages 2071, 3795.) The President also called attention to the seeming effect of the amendment in a letter to Senator Owen, reading as follows:

> I have been a good deal disturbed to learn of the proposed amendment to the Federal Reserve Act which seems to contemplate <u>charging the Federal reserve banks for payment of checks cleared by them</u>, or charging the payee of such checks passing through the reserve banks with a commission. I should regard such a provision as most unfortunate and as almost destructive of the function of the Federal reserve banks as a clearing house for member banks, a function which they have performed with so much benefit to the business of the country.
>
> I hope most sincerely that this matter may be adjusted without interfering with this indispensable clearing function of the banks. (P. 4083.)

In conference, apparently as the result of the letters of the Governor of the Federal Reserve Board and the President, the proviso took its present form, two changes being made by the conferees: First, the charges which member or nonmember banks may make were made subject to "to be determined and regulated by the Federal Reserve Board"; and second, the final clause was added, "but no such charges shall be made against the Federal reserve banks"

In presenting the conference report to the Senate, Senator Owen emphasized the importance of not interfering with the clearing functions of the Federal reserve banks, explained that under the proviso as amended

> the banks can charge each other for making these accommodations if they like, and they can adjust that to their own satisfaction with one another, without troubling the reserve banks,

and apparently conceded that State banks not connected as members or depositors with the Federal reserve system could not be subjected to Federal legislation. (P. 4083.)

Mr. Glass in presenting the report to the House said:

> The Congress has no control whatsoever over nonmember banks. It can not regulate their charges and will not regulate them if this Hardwick amendment should prevail. * * * This House has no control over the nonmember bank in this matter. Even the Federal Reserve Board has no control over their operations unless they voluntarily join the voluntary collection system established by the Federal Reserve Board. (P. 3794.)

and further

> No nonmember bank thatdoes not voluntarily join the collection system established by the Federal Reserve Board will be specifically affected. No law that we pass here can directly affect them. The only way they can be affected is incidental. (P. 3795.)

It thus seems clear that the proviso was understood by Congress as designed to protect the clearing functions of the Federal reserve banks and not directed at State banks which have no connection as members or depositors with the Federal reserve system and upon which it was considered the effect of the proviso could be only incidental.

It may be argued and is probably true that the proviso will necessarily affect the practice of State banks, though not members or depositors, as to making charges for the payment of checks drawn upon them. With the concentration of reserve balances in Federal reserve banks as required by the Federal Reserve Act, the Federal reserve clearing system may offer the only adequate and convenient facilities for clearing or collecting checks drawn upon banks at a distance, and depositors may find it inadvisable to maintain accounts with banks upon which checks cannot be cleared or collected by the use of these facilities.

The Federal Reserve Act, however, does not command or compel these State banks to forego any right they may have under the State laws to make charges in connection with the payment of checks drawn upon them. The Act merely offers the clearing and collection facilities of the Federal reserve banks upon specified conditions. If the State banks refuse to comply with the conditions by insisting upon making charges against the Federal reserve banks, the result will simply be, so far as the Federal Reserve Act is concerned, that since the Federal reserve banks cannot pay these charges they cannot clear or collect checks on banks demanding such payment from them.

From what has been said it follows that in my opinion the limitations contained in Section 13 relating to charges for the collection and payment of checks do not apply to State banks not connected with the Federal reserve system as members or depositors. Checks on banks making such charges cannot, however, be cleared or collected through Federal reserve banks.

Respectfully,

(Signed) T. W. Gregory,

Attorney General

The President,

The White House.