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AND FISCAL AGENT

ADDRESS REPLY TO
FEDERAL RESERVE BOARD

July 5, 1918.

X-1042

Dear Sir:

I inclose herewith, for your information, copy of a letter which has been addressed to Major-General Crowder, Provost Marshal General, together with memorandum of Counsel, asking that bank employees be not classified as engaged in non-essential work.

Very truly yours,

Governor.

C O P Y

July 3, 1918.

Major-General E. H. Crowder,
Provost Marshal General,
Washington, D. C.

S i r :

The Federal Reserve Board's attention has been called to the fact that in view of your announcement of June 21, 1918, which contains several important rulings explanatory of the recent "Work or Fight" regulations, some of your local Boards are disposed to classify bank clerks as engaged in a non-productive employment.

This office has received a number of letters from officers of Federal reserve banks, and other banks, indicating a very well-defined apprehension that the organization of the several banks may be so seriously disrupted as a result of this interpretation of your order it will be difficult, if not impossible, for the banks to successfully perform the services required of them by the United States Government.

The Federal Reserve Board does not desire to ask for ^{the} exemption from military service of any non-essential employee nor does it advocate the exemption of bank employees as a class. The forces of the several banks have already been materially depleted by the loss of men of the draft age and their places are being filled as rapidly as possible by older men or by women. The bank officials will continue to replace as rapidly as possible those who, in due course, are called to military service but if the forces of the banks are to be further depleted by a reclassification of those of draft age and by their transfer to other employments, it will be difficult for the banks to meet the increasing demands made upon them by the Government in the conduct of its fiscal affairs.

I am, therefore, taking the liberty of submitting for your consideration a memorandum prepared by Counsel for the Board which deals primarily with the public or Governmental services performed by the several banks. It is hardly necessary to emphasize the importance of maintaining the efficiency of the machinery used by the Government in the

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conduct of its fiscal affairs at the present time and the Board, therefore, hopes that upon consideration of all the circumstances you may feel justified in instructing the local Boards not to treat bank employees as engaged in a non-productive occupation or employment.

It is the understanding of this office that the provision contained in the regulations issued May 23, 1918, to the effect that "sales clerks and other clerks employed in stores and other mercantile establishments are engaged in non-productive employments" has been construed as including bank employees. If it was so intended it is hoped that you will consider the advisability of modifying this order so as to give the banks at least a reasonable time within which to reorganize their forces if you do not feel justified in classifying bank employees as engaged in a productive occupation or employment.

Respectfully,

W. P. G. HARDING

Governor.

C O P Y

July 3, 1918.

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Status of bank employees under selective service regulations issued by the Provost Marshal General, May 23, 1918.

MEMORANUUM FOR THE BOARD:

Under regulations issued by the Provost Marshal General,

"Sales clerks and other clerks employed in stores and other mercantile establishments are engaged in nonproductive employment."

The question arises whether banks should be treated as coming within the class of "Other mercantile establishments". This, of course, depends upon whether the Provost Marshal General intended this language to be so construed. As the business engaged in by banks under existing circumstances differs materially from that engaged in by ordinary private mercantile establishments, it may reasonably be argued that the Provost Marshal General did not intend to classify banks as a nonproductive occupation, but the regulations should, of course, be interpreted by his office.

Status of Banks created by Congress.

The constitutionality of the Act of Congress which created the first bank of the United States, was sustained on the ground that a bank is an instrumentality which may be used to aid the Government in the conduct of its fiscal affairs. (McCulloch v. Maryland, 4 Wheat, 316, 401; Osborn v. U. S. Bank, 9 Wheat, 738, 861.) The constitutionality of the Act creating national banks has been sustained on the same ground. (Farmers National Bank v. Dearing, 91 U. S. 29, 33.)

Banks created by Congress are not, therefore, organized solely for the benefit of their stockholders or the community which they serve. In the present emergency the services performed for the Government are not merely incidental to the private operations of the bank, but the converse is a more accurate statement of the situation; that is to say, the private operations of the bank are more or less incidental to the fundamental purpose for which they were created, viz: to assist the Government in the conduct of its fiscal affairs. This is, of course, true of national banks created by the Act of 1864, which Act contains the express provision that that all national banking associations "shall perform all such reasonable duties as depositaries of the public money and financial agents of the Government as may be required of them".

It is especially true of the Federal reserve banks which are also expressly authorized and required to act as fiscal agents of the Government and the earnings of which over and above a certain amount are paid to the Government in lieu of a franchise tax.

Prior to the passage of the Federal Reserve Act, approved December 23, 1913, it is true that the national banks were called upon to perform only limited services for the Government in connection with the collection and disbursement of Government revenues. Since the outbreak of the war in Europe, however, the demands made by the Government on Federal reserve banks, national banks, State banks and trust companies, have been constantly multiplied, and at the present time the Government is utilizing the services of nearly all banks in the conduct of its fiscal affairs.

Services performed by the Banks for the Government.

Since our entry into the war, it has been necessary for the United States Government to borrow from its citizens many billions of dollars to be used in aiding our allies, in building up our Army and Navy, and in placing us on a war footing.

By various acts of Congress, the Secretary has been authorized to sell to the public United States Bonds, certificates of indebtedness, war savings stamps and thrift stamps.

In order to effect these sales it was first of all necessary to create a market in the United States for Government securities. A very large proportion of those outstanding at the beginning of the war was held by national banks and other banking institutions. All foreign markets were, of course, closed, as each country had to dispose of its own securities. The investing public in the United States had little experience in investments of this sort, and it was necessary for the bankers to undertake a very large part of the work in conducting the various Liberty Loan Campaigns that have resulted so successfully. In this work the banks have been called upon (a) to make subscriptions and to purchase bonds for their own account; (b) to receive subscriptions from the public and to sell and deliver United States securities as agents of the Government; (c) to collect the purchase price of securities sold; (d) to act as depositaries of public funds; (e) to keep an accurate account of all transactions engaged in for the Government.

War Finance Act Approved April 5, 1918.

It is, of course, obvious that the sale of such large amounts of Government securities necessarily absorbed a very large part of the resources of the investing public. The Capital Issues Committee was accordingly created, to pass upon the question whether or not the sale of any securities other than Government securities, offered to the public, was compatible with the best interests of the United States; that is to say, was

the company or firms offering such securities engaged in a business which contributed directly or indirectly to the success of the war.

The War Finance Corporation was also created, with power to make loans upon securities which are not eligible for purchase or rediscount by the Federal reserve banks, and the securities so purchased are held by the corporation as collateral security for bonds issued by the corporation and sold to the public in order to provide additional funds for financing enterprises that are necessary to the Government in the conduct of the war.

Federal reserve banks are authorized to act as fiscal agents for the War Finance Corporation and these banks and the member banks of the Federal Reserve System are called upon to perform services both for the Capital Issues Committee and the War Finance Corporation. These services involve making reports as to issues of securities, acting as custodian of securities; and necessitate keeping of additional accounts and records and the employment of additional clerks.

Espionage Act Approved June 15, 1917; Trading
With the Enemy Act Approved October 6, 1917.

The Acts of Congress known as the Espionage Act and Trading With the Enemy Act, contain provisions regulating the exportation of gold or currency and make it possible for the Government to exercise the control over foreign exchange transactions and transfers of credit or securities for foreign account.

Under these acts persons desiring to export gold or currency are required to obtain a license from the Federal Reserve Board, which licenses are issued through the various Federal reserve banks. Dealers in foreign exchange are required to obtain a license trade certificate from the Federal Reserve Board through the Federal reserve banks and to make detailed reports of all transactions. This entails the employment of additional clerks and employees and the keeping of additional accounts.

Demand for Experienced Clerks and Accountants.

In the performance of ^{nearly} all of the services required by the Government, it is necessary for the banks to select their employees from those who have had experience in accounting and the accurate keeping of records. It is inevitable that many of the employees must be entrusted with the handling of money and securities of value and great care must be used in the selection of such employees. With the constantly increasing demands made upon the banks, it is difficult for the officers to train those without previous experience. Women are being used for much of this work, but the local laws limiting the number of hours they may be employed, makes it necessary to increase the number of employees in many instances.

Under the circumstances, it is respectfully submitted that the work engaged in by the banks is of vital importance to the United States Government and differs materially from that of the ordinary mercantile establishment.

Respectfully,

M. C. ELLIOTT.

Counsel.

*Printed according to transmission
with 7-1049*

FEDERAL RESERVE BOARD

WASHINGTON

July 6, 1918.

Dear Sir:

In the Bulletin for April, 1918, the Federal Reserve Board published a statement setting forth the reasons why, in its opinion, a gradual but consistent curtailment of nonessential credits is necessary, and urging the banks and trust companies of the country to do whatever they could in the exercise of a reasonable discretion to restrict credits which are clearly not needed for the prosecution of the war or for the health and necessary comfort of the people.

On June 12, the Secretary of the Treasury addressed a letter to all banks and trust companies, announcing his financial program for the ensuing six months which involves the sale to and through banks of approximately six billion dollars of Treasury certificates of indebtedness, in installments of not less than \$750,000,000 every two weeks between June 25 and the first of November. In this letter each bank and trust company was requested to invest in these certificates an amount equal to approximately 2½ per cent of its gross resources, or a total of 5 per cent for each month. Announcement was made at the same time that there was in contemplation an issue of two billion dollars of certificates of appropriate maturities in anticipation of income and excess profits taxes, for sale more particularly to taxpayers, and that the amount of the regular semimonthly sales of certificates of indebtedness would be reduced in proportion to the extent to which these tax certificates are taken by the public.

The banking institutions have responded most generously to the appeal of the Secretary of the Treasury. Throughout the country they have pledged themselves without hesitation to subscribe to their allotment, and the result of the initial offering which has just been closed—a subscription of \$838,000,000 in response to a request for not less than \$750,000,000—is evidence of the splendid patriotism of those who direct our national and State banking institutions. The Board hopes that succeeding issues will be subscribed as readily and in the same patriotic spirit.

The Federal Reserve Banks will be prepared to place their facilities—directly or indirectly—at the disposal of such subscribing banks as may legitimately need assistance in taking their allotments. The Board, however, feels in duty bound to reiterate that the banks can render a greater service to the country in this connection, not merely by subscribing their allotments and by using the rediscounting facilities of the Federal Reserve Banks in making payments, but by providing the necessary funds for meeting payments for certificates of indebtedness purchased, by employing for this purpose the accretion of new deposits, and by utilizing the funds that may be made available by a judicious curtailment of credits asked for non-essential purposes.

In order to prosecute the war successfully, the Government is compelled to issue obligations to provide for its large expenditures which involve waste and destruction rather than a permanent addition to the national wealth. This process in itself tends to inflation, and contributes to a rapid increase in the price of necessities. Abnormal demands by the Government, unavoidable and necessary in the present circumstances, must be counteracted by greater economy on the part of the civilian population which must decrease, by combined effort, the normal waste incident to domestic life and business pursuits. There is not an unlimited supply of credit or of goods, or of man power. Wherever possible all such resources should be conserved and set aside for the use of the Government. Credit extended for nonessential purposes involves the use of labor, of transportation, of material and reserves which ought to be kept free for the use of the Government. Unrestricted credit involves unnecessary competition with the Government, and needlessly advances prices, besides impeding and delaying Governmental operations.

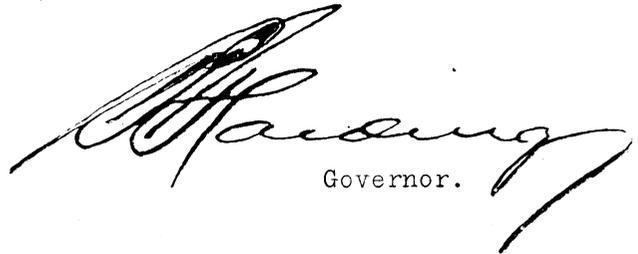
"Business as usual" and "life as usual" are impossible at a time when the supreme business of the country is war, and can not be approximated without interfering with the work of the Government and inflicting serious harm upon the Nation as a whole. The staying power of the country in this emergency depends upon the extent of its resources in men, goods, and gold. An unnecessary use of credit, a needless recourse to the discounting facilities of the Federal Reserve Banks, weakens proportionately the gold reserve of the United States—the financial backbone of the entire allied group. Whoever wastes the raw material and manufactured products of the country adds to our financial burden by increasing the amount the United States must import from other countries and by decreasing, at the same time, the volume of goods that should be available for export purposes—the best means of paying for the goods acquired from abroad.

Conservation of our commodities and of our gold—preservation of our economic strength—is of the greatest importance in making provision for the period of readjustment which will follow the reestablishment of peace. The country having the largest supply of goods and gold available at the end of the war will find itself in the best strategic position for controlling the markets of the world. The Board wishes to point out, also, that by refraining from buying luxuries, and by restricting the use of necessities to the actual requirements of health and reasonable comfort, we can create a reserve purchasing power which will be of the greatest value in bridging over our industries during the period of reaction and reconstruction which must follow when war industries are transformed into peace industries. An intelligent and prudent use of credit, therefore, will be an important factor in strengthening the national resources during the period of the war, in aiding its successful prosecution, and in maintaining the economic strength of the country for the time of rapidly changing conditions which will come when the war has been won and the millions of men in our armies are returning to the employments of peace.

Thus, by giving your cooperation now in the effort to conserve national resources by the exercise of discriminating judgment in granting credits, you will also do your part in averting the danger of unemployment which is apt

to follow a treaty of peace. The Board appreciates the difficulty of laying down a general rule for defining essentials or the degree in which any enterprise is essential, and requests that its remarks on this subject in the April issue of the Bulletin be read again. The Board can not suggest specific ways in which credit should be conserved or unnecessary expenditures curtailed, as each banker must determine this for himself after conferring with the business men of his community and after a careful study of his local situation. Reasonable discretion should be exercised, and, drastic steps calculated to bring about hardships or embarrassments or work injustice should be avoided, but the banks should divert the use of their credit more and more into productive fields, where its employment will result in augmenting the national resources.

Respectfully yours,



Governor.

To the President
of the Bank or
Trust Company addressed.