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ADDRESS REPLY TO  
FEDERAL RESERVE BOARD

June 10, 1919.

X-1576

Subject: Reclassification of Reserve and Central Reserve Cities.

Dear Sir:

In section 13 of the Federal Reserve Act there is a clause which provides that "the organization of Federal reserve districts and Federal reserve cities shall not be construed as changing the present status of reserve and central reserve cities", and consequently in the exercise of the power conferred upon the Board in paragraph (e) of section 11, "to add to the number of cities classified as reserve and central reserve cities under existing law in which national banking associations are subject to the reserve requirements set forth in section twenty of this Act; or to reclassify existing reserve and central reserve cities or to terminate their designation as such", the Board did not change the status of the three central reserve cities, New York, Chicago and St. Louis, which had been central reserve cities for many years prior to the passage of the Federal Reserve Act. Consequently member banks in these cities are obliged to carry reserves of 13% against their demand deposits while banks in the other cities having Federal reserve banks, which were also reserve cities under the old law, need carry only 10% reserves against their demand deposits.

More than two years ago the Board announced its policy of classifying all cities in which branches of Federal reserve banks might be located as reserve cities, and accordingly member banks in all such cities are now required to carry 10% reserves against their demand deposits. It is obvious, however, in view of the change in reserve requirements made by the Federal reserve law as originally enacted and more particularly by the amendment of June 21, 1917, that the old classification of reserve and central reserve cities has become obsolete. The member banks in St. Louis, for example, have no greater opportunity for expansion than have those of Boston, Philadelphia and Cleveland, all of which cities exceed St. Louis in population, but because of the previous status of St. Louis as a central reserve city they are required to carry 13% reserves against demand deposits while those of the other three cities named need carry only 10%.

The Board is considering the advisability of reclassifying the list of central reserve and reserve cities, and as all twelve cities in which Federal reserve banks are located have become the financial centers of their respective districts, it seems that there may be good reasons for classifying

them all as central reserve cities. Such action would increase the reserve requirements in nine of the Federal reserve cities from 10% to 13% as against demand deposits. It is not the purpose of the Board to take hasty action, and if the Board should determine to make the change, it would give ample notice.

The present law does not require nor permit any part of a member bank's lawful reserve to be carried in its own vault, and the amount of cash carried by a member bank is optional with it. A member bank in a Federal reserve city can, therefore, afford to let its vault cash run down to a minimum for the reason that it can replenish its cash on a few minutes notice, while banks located at a distance feel that prudence demands that they carry a larger amount of vault cash as time is a necessary factor in adding to their cash holdings in case of unexpected need or emergency. The same observations apply to cities which have branches of Federal reserve banks, and it may be argued that those cities also should be classified as central reserve cities.

The Board feels, however, that it must consider the effect upon the member banks and particularly upon State banks which have become members of the system and which can exercise their statutory privilege of withdrawing on six months' notice. If it should be deemed advisable to classify branch bank cities as central reserve cities, it might be well to give them longer notice than in the case of Federal reserve bank cities of such intention in order that the member banks in any branch bank city may have ample time to decide whether to increase their reserves or to have their branch discontinued.

The Board is receiving a good many applications for the establishment of additional branches, and perhaps if it were known that all branch bank cities would be classified as central reserve cities the desire to have additional branches established would not be so keen.

This is a confidential letter and in discussing it with your executive committee and your directors you should have it so understood. It is important, however, that the matter be carefully considered before any action is decided upon, and you are requested, after conferring with your officers and directors, to write the Board stating frankly the consensus of opinions expressed. You are also invited to give a full and free expression of your own views.

Very truly yours,

Governor.

LETTER SENT TO CHAIRMAN OF ALL BANKS