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ADDRESS REPLY TO  
 FEDERAL RESERVE BOARD

## FEDERAL RESERVE BOARD

WASHINGTON

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 W. M. INLAY, FISCAL AGENT

November 7, 1919.

X-1719

Subject: Recommendations made at Conference of Federal Reserve Agents, October 22-24, 1919.

Dear Sir:-

The Federal Reserve Board has considered the recommendations of the Federal Reserve Agents' Conference, held in Washington, Oct. 22-24, 1919, copy of which is attached hereto, and submits the following comment with reference to certain recommendations made.

FEDERAL RESERVE AGENTS' SPECIAL FUNCTIONS

(a) NOTE ISSUE

(3) Redemptions.

The Federal Reserve Board wishes to urge upon the Federal Reserve Agents the necessity for closer sorting of unfit Federal Reserve notes forwarded to Washington for redemption, and requests that this matter be brought to the attention of the officers of the Federal Reserve Banks. At the present time, about \$11,000,000 of Federal Reserve notes are being shipped to Federal Reserve Agents from Washington daily, while the output of the Bureau of Engraving and Printing is only about \$7,000,000. In order to meet the heavy fall demand for currency, and furthermore, in the interests of economy, it is necessary that Federal Reserve Banks sort their notes much closer and forward to Washington for redemption only those notes which are unfit for further circulation. In a recent communication which the Board received from the Treasurer of the United States, the statement was made that it was estimated the remittances received from some of the Federal Reserve Banks contained from 35 to 60% fit notes.

(4) Design of Federal Reserve Notes.

The Board has under consideration the recommendation that steps be taken to change the design of Federal Reserve notes in order to make fraudulent use more difficult. The Board desires, however, that no publicity be given to this matter, feeling that perhaps more unscrupulous persons might be tempted to engage in counterfeiting or raising Federal Reserve notes.

(g) RELATIONS WITH MEMBER BANKS.

(3) Proper use of system by members - can a program be formulated?

The Board is in accord with the expression of opinion that personal contact with member banks is very desirable, and feels that each Federal Reserve Bank should keep in personal touch with as large a number of its member banks as possible, the method to be determined by each Federal Reserve Bank to meet its own local conditions.

(h) RELATIONS WITH NON-MEMBER BANKS.

(1) What can be done to increase membership?

The Federal Reserve Board approved the recommendation "that an energetic and organized campaign should be immediately inaugurated in every Federal Reserve District to secure membership in the Federal Reserve System of eligible and desirable state banks", and believes this to be an opportune time in the majority of districts to start such a campaign, in view of the missionary work which has already been done by the officers of Reserve Banks in their par point campaigns; and believes that a still more intensive state bank membership campaign should be launched immediately following the first of the year; and concurs with the recommendation that the campaign should also embrace educational work among member banks to acquaint them with the value and the proper use of the facilities of the Federal Reserve System.

FEDERAL RESERVE BANK POLICIES

(a) PAR POINT CAMPAIGN.

The Board concurs with the recommendation that on January 1, 1920, those states in which there are relatively few non-par remitting banks, be placed on the par list in entirety, and that checks of those banks which continue to be unwilling to remit at par, be collected by agents, express companies or otherwise.

- (a) 2. "We deem it feasible and desirable to obtain cooperation and action from the clearing houses throughout the country in modifying schedules wherein the time element acts in a discriminating way against certain points and sections of the country."

The Board concurs in the above recommendation and desires that Federal Reserve Agents endeavor to obtain cooperation and action from the clearing houses in their districts with a view to modifying schedules wherein the time element acts in a discriminating way against certain points and sections of the country.

(h) COMPENSATION OF EMPLOYEES.

(1) Wages and Bonuses.

The Board has considered the recommendation on the above subject, but in view of the fact that the matter will be discussed fully at the Conference with the Governors on the 19th instant, does not deem it advisable to make any further comments at this time.

Very truly yours,

Governor.

Letter to Chairmen of all F.R. Banks.

X-1719a

There follow the recommendations of the Federal Reserve Agents to the Federal Reserve Board, adopted by the Federal Reserve Agents' Conference held in Washington October 22 - 24, 1919.

FEDERAL RESERVE AGENT'S SPECIAL FUNCTIONS

(a) NOTE ISSUE

(1) Discussion of expansion and contraction.

Expansion and contraction in Federal Reserve notes is dependent in general on the price level. While in agricultural districts there has been expansion and contraction to meet seasonal demands, the extent of contraction is still dependent on the price level, for the figures show as the level of prices increases Federal Reserve notes in circulation remain after each seasonal fluctuation at a higher level.

Unless some direct method can be devised to decrease the price level there can be no permanent contraction of Federal Reserve notes, except through curtailment of public demand through economy and savings.

(2) Supply of coin and currency.

In those districts where it is generally known that the Federal Reserve Bank supplies currency free of all transportation cost, the Federal Reserve Bank supplies its district almost completely.

It is suggested that if a campaign of education is conducted in all districts so that the member banks know they can get currency without cost from their Federal Reserve Banks each Federal Reserve Bank will supply its district and add to its popularity, and this service can be used as an argument for enhancing the value of membership. In some of the large cities correspondent banks are shipping out currency to member banks in other districts, a practice which this educational work will tend to discourage.

(3) Redemption.

The volume of shipments for redemption by member banks and by Federal Reserve Banks can be reduced by a closer sorting of unfit Federal Reserve notes in all Federal Reserve Banks and also by demands on the Treasury Department for currency in Federal Reserve districts being supplied by local Federal Reserve Banks rather than by shipments of Federal Reserve notes of other Federal Reserve Banks into a Federal Reserve district.

(4) Design of Federal Reserve notes.

It is recommended that immediate steps be taken to improve the design of Federal Reserve notes in order to make fraudulent use more difficult, and to expedite sorting.

The conference submitted the following report for the information of the Board.

Mr. Chase reports as follows:

From a practical standpoint, I think the design on Federal Reserve notes could be improved by adopting two changes which I understand are the patented property of Edward B. Andrus of the Cosmopolitan Trust Company of Boston. He has perfected and patented an improved design for currency which embraces among other features the two following, which are of considerable merit:

1. That the figures on the smaller denominations of bills be larger than the figures on the larger denominations so that genuine figures from the larger denominations could not be torn off and pasted over the figures of the smaller denominations as has been done throughout the country of late on a large scale.
2. Mr. Andrus has perfected a design on the diagonal principle so that however it may be placed a note is always right side up. This does not improve the artistic appearance of the notes but it would be a tremendous practical advantage to people who actually handle currency, especially for banks such as ours, in which hours of labor are wasted in a day merely in arranging notes right side up and right side to.

## (e) CLAYTON ACT

- (1) Should existing permits be revised?

It is the judgment of this conference that the policy of the Federal Reserve Board in determining what is substantial competition under the Clayton Act amended has resulted satisfactorily and that no review of present permits is necessary except in those cases where a decided and known change has taken place in the nature of the business of the institutions with interlocking directors.

## (g) RELATIONS WITH MEMBER BANKS

- (1) Services, present and prospective, and their cost.

The service afforded by the Federal Reserve Banks is valuable to member banks and is, or should be, an inducement to membership on the part of nonmembers. Dividends are limited

by law to six per cent, a fair return on capital investment. Interest on balances is very properly disallowed. Nevertheless the present large earnings and prospective profits are, to a large extent, the result of use of the capital and reserves of member banks, and such member banks should, therefore, be entitled to the largest possible return in the form of service dividends. There seems to be no reason to believe that the cost of operation should in the future advance beyond a normal increase due to natural growth, and therefore, there is nothing to prevent the continuance of such dividends in service.

(2) Are any members considering withdrawing?

A number of banks have already withdrawn from membership and it appears that some others have filed application for withdrawal. Some banks having indicated a disposition to withdraw have concluded not to do so after a personal visit from an officer of the Federal Reserve Bank, it being demonstrated in these cases that the dissatisfied member had an inadequate conception of the real purpose of the system and a lack of comprehension of benefits to be obtained through proper use of the facilities offered.

In general, it appears that withdrawals may be classified under two groups -- first, those who wish to make membership merely a source of direct and increased profit through excessive use or abuse of the privileges granted, (which members are of no benefit to the system); and second, such members as come in through purely patriotic motives, having little or no occasion to use the rediscounting privileges, and therefore figure that continuing membership means lessened profits without compensating benefits. It is likely that in such instances, or most of them, a personal visit by some well qualified representative of the Federal Reserve Bank would result in the abandonment of intention to withdraw.

## (3) Proper use of system by members -- can a program be formulated?

It is impracticable to frame a definite program for universal application, for each district has its own peculiar conditions which must be dealt with accordingly. However, in important respects a proper use of the facilities of the system can be brought about and should be encouraged on the part of member banks throughout the country without abuse of the privilege. It is manifest that many member banks are as yet without proper knowledge in these matters. It is suggested that personal touch and acquaintance properly followed up may open the way for correction of this situation. The particular method, however, must be worked out in each district according to local conditions.

## (h) RELATIONS WITH NONMEMBER BANKS.

(1) What can be done to increase membership?

We are convinced that personal contact and discussion furnishes the most practical method of increasing membership. The appeal to patriotism alone is no longer effective. Desirable nonmember banks are already largely informed, in a general way, at least, as to the system. The best advertisement is a satisfied customer. If our present members receive satisfactory service, they will recommend it to others.

We believe that an energetic and organized campaign should be immediately inaugurated in every Federal Reserve District to secure membership in the Federal Reserve System of eligible and desirable state banks and that any proper and legitimate expense necessary to reasonable success should be incurred. Included in this effort and as an aid to its accomplishment there should be a general and intensive campaign to acquaint member banks with the value and proper use of the facilities of the Federal Reserve System.

## (i) RELATIONS WITH PUBLIC.

(1 - 2) We believe in publicity, but we also believe that it should be specialized publicity, and that it should be directed from time to time toward the objectives that we are anxious to reach. In banks, the directors as well as the officers, should be listed and gone after. A mailing list of the district leaders in trade, industry and agriculture should be kept and added to from time to time for this purpose.

FEDERAL RESERVE BANK POLICIES

## (a) PAR POINT CAMPAIGN.

In preparing this report the Committee had before it reports made yesterday by the several chairmen of the results of the campaign for par collections in their several districts. Two things were developed by these reports.

(1) The proposition of the Federal Reserve Board to insist upon the use of symbols on checks had given an impetus to the campaign, since reserve banks as well as other banks foresaw the difficulties in its practical operation together with the discrimination against non-remitting banks that the use of the symbols would provoke.

(2) Satisfactory progress is being made in a majority of the districts, and it appears that when non-remitting banks were notified that on a fixed date checks on themselves would be put on the par list and collected by agents, express companies, or otherwise, over 80 per cent of the banks thus notified signed agreements to remit at par.

We recommend that in States where there are relatively few non-remitting banks, such non-remitting banks be notified that not later than January 1st, their checks will be put on the par list and collected in the manner heretofore mentioned; that in those States that have a large number of non-remitting banks, such banks be notified that not later than March 1st checks on themselves cleared through the Federal Reserve Banks will be collected at par.

Such action is justified since Federal Reserve Banks are paying the cost of currency shipments.

While we do not believe the symbol plan is necessary in States that are entirely on the par list, we recommend that the Board do not withdraw at this time its intention of using such plan.

In view of the apparent ambiguity of that part of Section 16 of the Federal Reserve Act relating to the fixing by the Federal Reserve Board of charges to be made on checks cleared through Federal Reserve Banks, we further recommend that the Board defer promulgating a regulation of this kind until at least after the completion of the campaign for par points. It is almost impossible to make a fair and uniform charge that will include interest for transit time as well as compensation for risk and service. These latter charges depend upon the varying conditions in the several districts together with the value of the customers' endorsement and account.

(Mr. McCord and Mr. Rich wished to be recorded as voting against this paragraph.)

We deem it feasible and desirable to obtain cooperation and action from the clearing houses throughout the country in modifying schedules wherein the time element acts in a discriminating way against certain points and sections of the country.



(b) AMENDMENTS.

## (1) Reserve and Net Deposits.

There does not appear to be any demand at the present time for a revision of the reserve situation or the practice of arriving at the net deposits upon which reserves are to be calculated that would warrant your Committee in recommending changes without more careful study and analysis of the situation than the limited time given the Committee to discuss the subject would allow.

It would be impossible, both from the National Bank and member State Bank standpoint, to have changes recommended, especially those requiring legislative action, without the greatest study and care as to the effect of those changes on the different classes of banks and commercial, industrial and agricultural interests in different sections of the country.

(c) RATES

Of the topics assigned to the Committee there has only been opportunity to consider briefly the question of the present expansion of credit and what methods of control of credit may be successfully used by the Federal Reserve Banks in view of the Government's past and prospective financial program.

The increasing demands for credit appear to come (a) from the higher costs of commodities and labor in the production and distribution of goods, caused by excess of demand over supply, and (b) from the higher prices of securities, land, and other forms of fixed property, as well as of many commodities, caused by active speculation all over the country.

The normal check for the Federal Reserve Banks to use is a higher discount rate. But in the opinion of your Committee the conditions prevailing at home and abroad are so abnormal as to render this method not wholly effective of itself. The European countries are extremely short of goods, and we ourselves have not yet been able to satisfy the accumulated demand for goods resulting from two years of patriotic self-denial on the one hand and a more widely diffused spending power on the other. Furthermore, international trade is extremely unsettled and all the important European exchanges are heavily in our favor. It is evident that the use of credit for producing the goods of which the world is short should not be unduly curtailed, and it seems equally evident that the immoderate use of credit by those engaged in speculation in securities, land and commodities to force prices higher is not only undesirable from its effect on the cost of living but is laying the foundation for future collapse and depression.

Some increase in the bank rate, however, seems the necessary first step in any program for the restraint of undesirable credit expansion, as an indication to the banks that, with the war financing of the Government now on a declining

(c) RATES (continued)

scale, the Federal Reserve Banks may be expected henceforth to function normally. But such increase, which need not be large, or uniform in all districts, would be ineffective unless accompanied by a campaign, undertaken gradually and with great discretion to secure greater moderation by banks in the extension of credit for speculative and other undesirable purpose.

The fact that Government financing is on a descending scale no longer seems to require such a degree of uniformity in Federal Reserve Bank rates as prevailed during the war, when the Liberty bond rate necessarily overshadowed all others and practically dictated uniformity. It is the belief of your Committee that rates at the several banks need no longer be established either simultaneously or at similar levels.

Your Committee is of the opinion that the present preferential rate on government paper has served its purpose and may now or shortly be modified or withdrawn, and that in future rates at which government secured paper is taken by Federal Reserve Banks, <sup>should</sup> be such as not to permit rediscounting at a profit over the coupon or interest rate.

(h) COMPENSATION OF EMPLOYEES

## (1) Wages and Bonuses.

Bonuses, as such, are ordinarily given by commercial banks, manufacturing and industrial institutions, as an act of grace, or as a bounty or in appreciation of loyal and faithful service. In concerns conducted for profit, when the gains of the business have been large and the profits are subject to distribution in the reasonable discretion of its principal owners, there can not only be no objection to the granting of this bonus to employees, but the practice may often be commended. It is believed, however, that the reasons underlying the granting of bonuses by concerns organized and conducted for profit can have no application to Federal Reserve Banks whose earnings are subject to definite distribution under the law. Bonuses in Federal Reserve Banks can only be justified and upheld as in the nature of readjustment of salary if and when made necessary by unusual conditions, such as now obtain, and which have obtained now for a considerable time. We believe that the correct rule should be for each Federal Reserve Bank to fix at stated and not too frequent intervals the salary of each employee and this with some reference to the scale of pay for similar work prevailing in the section where such bank is located, but more with special reference to the nature of the employee's work, and the experience, ability and fidelity of the employee. We think it poor economy to fix salaries at unreasonably low figures and manifestly wrong to pay a wage unreasonably high. There is a middle ground where salaries would be fixed in a spirit of consideration of the value of the services of the employee and in a like spirit of exact justice to the bank. Under normal conditions we believe all compensations should be fixed in definite salaries, with no promise, expressed or implied, that a bonus would be paid.

(h) COMPENSATION OF EMPLOYEES continued

(1) Wages and Bonuses. continued.

We believe, however, that under present conditions the payment of reasonable and substantial bonuses is required and demanded both as an act of justice to the employees and in the interest of the Federal Reserve Banks. The universal and rather unexpected increase in the cost and expense of living, including an unprecedented increase in the cost of housing, makes the granting of fair bonuses seem an act of needed justice to the employee. The competition for good clerical help, not only among banks but with railways, manufacturing and industrial concerns, and the general granting by practically all such businesses of considerable and sometimes generous bonuses seems to make it almost a matter of necessity for Federal Reserve Banks to follow a somewhat similar course if they are to maintain their organizations unimpaired and to retain their help with any feeling of satisfaction.

We do not believe it practicable to fix any scale of bonus payments which shall be uniform among all banks. The scale of bonuses to be paid should be left to the sound discretion of the Boards of Directors of the several Federal Reserve Districts, subject, of course, to the control and approval of the Federal Reserve Board. We think that it could well be stated in the letter accompanying the transmission of such bonus checks that the payment of same under present conditions was not to be understood as furnishing any precedent for the future.

(Mr. Hardy voted "no" on this report.)