

EX OFFICIO MEMBERS

CARTER GLASS

SECRETARY OF THE TREASURY
CHAIRMANJOHN SKELTON WILLIAMS
COMPTROLLER OF THE CURRENCY

ADDRESS REPLY TO

FEDERAL RESERVE BOARD

FEDERAL RESERVE BOARD

WASHINGTON

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W. M. IMLAY, FISCAL AGENT

February 9, 1920.

X-1827

Subject: Acceptances of the Continental
Guaranty Corporation.

Dear Sir:-

On December 15, 1919, the Federal Reserve Board addressed to you a letter reading as follows:

" The Federal Reserve Board has been advised that the Continental Guaranty Corporation of New York has widely circulated circulars and forms relating to a plan which it has devised to finance the purchase of automobiles by local dealers from manufacturers, and the Board has received from several of the Federal Reserve Banks inquiries not only as to the nature and scope of this plan but also as to whether or not paper drawn and accepted thereunder is eligible for rediscount as a bankers' acceptance.

" The Board is of the opinion that technically the drafts described, when accepted by the Continental Guaranty Corporation, come within its definition of a bankers' acceptance set forth in its regulations and as such are technically eligible for discount provided that they comply in other respects with the terms of the law and the regulations of the Federal Reserve Board.

" The Board has been advised further that its letter of July 22, 1919, addressed to the Continental Guaranty Corporation, stating that its acceptances of the kinds described would be eligible for discount provided, of course, that they comply with the various terms of the Federal Reserve Act and the regulations of the Board, has been widely distributed with its other circulars and forms among banks and bankers throughout the country. Because of the very general misunderstanding which evidently has resulted, the Board wishes to state that this letter of July 22, 1919, was not in fact and should not in any way be construed to be an expression of its approval of the merits or desirability of the paper as an investment either by the reserve banks or their member banks, and the Board regrets that it has been circularized in such a manner as

to give undue advertising value to the plan of the Continental Guaranty Corporation which it accompanies.

" Federal Reserve Banks are, of course, aware that it is their right and duty carefully to consider the merits or bankable risk attached to any paper presented either for rediscount or purchase and in their own discretion to accept or refuse the paper on the basis of that consideration. The Board believes, however, that many member banks may fail to appreciate that technical eligibility does not of itself imply desirability and you are therefore requested, whenever opportunities afford themselves, carefully to indicate this distinction to member banks interested with a view of correcting what might otherwise be a wrong impression of the purpose and effect of the Board's letter referred to above."

Because of the Board's statement in the above letter to the effect that it had been advised that its letter of July 22, 1919, addressed to the Continental Guaranty Corporation, had been " widely distributed" with the other circulars and forms of that Corporation among banks and bankers throughout the country, the Continental Guaranty Corporation in a letter addressed to the Board under date of January 15, 1920, has explained that although " in a small number of cases specific reference" has been made by it to the Board's letter of July 22 in correspondence with banks who have " asked the direct question of our authority for the eligibility of the drafts or has expressed doubt as to their eligibility" and although in one particular instance a copy of the Board's letter was forwarded to a bank and although a photostatic copy of the Board's letter was given to each one of its twenty field representatives to show to any banker whenever the eligibility of the Corporation's acceptances is at issue, nevertheless " in no other case can any officer of the Corporation remember having sent out a copy of this letter to any one in correspondence." In concluding the Corporation stated that it " has never used the Board's letter of July 22, except in the ordinary and proper course of business unless such use has been by some one of the district representatives who has parted with his copy of said letter without authority and against the express prohibition of the officers of the Corporation and that therefore the Board was misinformed in the premises upon which its letter of December 15 to the Federal Reserve Banks was written."

The Board is, of course, glad to be advised that the Continental Guaranty Corporation itself has not, except in the cases recited, sent out a copy of the Board's letter to anyone in correspondence. In view of that explanation it is probable that most of the advices received by the Federal Reserve Board with reference to the use of that letter by the Corporation were based upon the photostatic copy which had been furnished by the Corporation to each of its twenty field representatives with express authority to show it to the interviewed banker whenever the eligibility of the Corporation's paper was at issue.

Independently, however, of the precise extent to or manner in which the Board's original letter was brought to the attention of banks and bankers throughout the country, the Board wishes to reaffirm its former opinion that its original letter of July 22, 1919, " was not in fact and should not in any way be construed to be an expression of its approval of the merits or desirability of the paper (of the Continental Guaranty Corporation) as an investment either by the reserve banks or their member banks," and that Federal Reserve Banks should indicate to interested member banks that a ruling by the Board as to technical eligibility should not of itself imply approval or disapproval of the merits of the paper.

Because of the fact, however, that the Continental Guaranty Corporation has stated in its letter, addressed to the Board, that "undoubtedly very great injury is being done to the credit of the Corporation with the banks who have received copies of or notice of the board's letter of December 15, " the board wishes to advise that, while its original letter of July 22, 1919, should not be construed in any way to approve the merits or desirability of the Corporation's paper, so also, its subsequent letter of December 15, quoted above, should not be construed to be an expression of the Board's disapproval of the merits or desirability of that paper. The purpose of that letter was solely to rebut any erroneous inferences that may have been drawn by banks or bankers receiving or seeing typed or photostatic copies of the Board's original letter passing upon the mere technical eligibility of the paper issued in accordance with a specified plan.

This letter is addressed to you in order that you might wherever possible correct any misunderstanding of that purpose that may exist.

Very truly yours,

Governor.

To Governors and Chairmen of all F.R. Banks.