FEDERAL RESERVE BOARD

WASHINGTON

X-3128
May 17, 1921.

SUBJECT: Supreme Court Decision in Par Clearing Suit.

Dear Sir:

There is enclosed for your information copy of the opinion of the Supreme Court of the United States in the case of the Georgia country banks against the Federal Reserve Bank of Atlanta.

Counsel calls the Board's attention to the fact that in this opinion the contention of the Federal Reserve Bank is upheld that the District Court of the United States has jurisdiction in the case but it denies the Federal Reserve Bank's motion to dismiss the plaintiff's complaint. Suit was brought by a group of non-member banks to enjoin the Federal Reserve Bank from collecting checks drawn on the country banks by having agents demand payment in cash in cases where the country banks declined to remit at par, the complaint alleging that the Federal Reserve Bank undertook the collection of such checks by presentation and demand of payment in cash with the intent of injuring the banks on which the checks were drawn. As the issue before the Supreme Court was merely whether, as a matter of pleading, the plaintiff's bill of complaint stated a cause of action, the decision of the Supreme Court is not a final determination of the litigation and the case will now be sent back to the District Court of the United States for the Northern District of Georgia for trial upon the merits. The opinion of the Supreme Court does not deny the legal authority of the Federal Reserve Bank to collect checks on non-member banks by making presentation thereof at the counter, but holds merely that non-member banks may be entitled to relief if they can prove that the Federal Reserve Bank malevolently intends to accumulate checks and present them in an oppressive manner for the sole purpose of injuring the banks upon which the checks are drawn.

As to the scope of the Supreme Court's decision, the court said:

> "The question at this stage is not what the plaintiffs may be able to prove or what may be the reasonable interpretation of the defendant's acts but whether the plaintiffs have shown a ground for relief if they can prove what they alleged."

In the opinion of Counsel, the Supreme Court's decision will not interfere with the present check clearing functions of the Federal Reserve Banks and those banks may continue, as heretofore, to collect checks drawn upon those banks which are listed upon the par lists.

Very truly yours,

(Enclosure)

G o v e r n o r.

CHAIRMEN OF ALL F.R.BANKS.

COPY X-3128a

SUPREME COURT OF THE UNITED STATES

No. 679 - October Term, 1920.

American Bank and Trust Company et al., Appellants, vs. Federal Reserve Bank of Atlanta, Georgia, et al.) Appeal from the United States Circuit Court of Appeals for the Fifth Circuit.

(May 16, 1921)

Mr. Justice Holmes delivered the opinion of the Court.

This is a bill in equity brought by country banks incorporated by the State of Georgia against the Federal Reserve Bank of Atlanta, incorporated under the laws of the United States, and its officers. It was brought in a State Court but removed to the District Court of the United States on the petition of the defendants. A motion to remand was made by the plaintiffs but was overruled. The allegations of the bill may be summed up in comparatively few words. The plaintiffs are not members of the Federal Reserve System and many of them have too small a capital to permit their joining it - a capital that could not be increased to the required amount in the thinly populated sections of the country where they operate. An important part of the income of these small institutions is a charge for the services rendered by them in paying checks drawn upon them at a distance and forwarded, generally by other banks, through the mail. The charge covers the expense incurred by the paying bank and a small profit. The banks in the Federal Reserve System are forbidden to make such charges to other banks in the System. Federal Reserve Act of December 23, 1913, c. 6, Section 13; 38 Stat. 263; amended March 3, 1915, c. 93; 38 Stat. 958; September 7, 1916, c. 461; 39 Stat. 752; and June 21, 1917, c. 32, Sections 4, 5; 40 Stat. 234, 235. It is alleged that in pursuance of a policy accepted by the Federal Reserve Board the defendant bank has determined to use its power to compel the plaintiffs and others in like situation to become members of the defendant, or at least to open a non-member clearing account with defendant, and thereby under the defendant's requirements, to make it necessary for the plaintiffs to maintain a much larger reserve than in their present condition they need. This diminution of their lending power coupled with the loss of the profit caused by the above mentioned clearing of bank checks and drafts at par will drive some of the plaintiffs out of business and diminish the income of all. To accomplish the defendants' wish they intend to accumulate checks upon the country banks until they reach a large amount and then to cause them to be presented for payment over the counter or by other devices detailed

to require payment in cash in such wise as to compel the plaintiffs to maintain so much cash in their vaults as to drive them out of business or force them, if able, to submit to the defendant's scheme. It is alleged that the proposed conduct will deprive the plaintiffs of their property without due process of law contrary to the Fifth Amendment of the Constitution and that it is ultra vires. The bill seeks an injunction against the defendants collecting checks except in the usual way. The District Court dismissed the bill for want of equity and its decree was affirmed by the Circuit Court of Appeals (November 19, 1920). The plaintiffs appealed, setting up want of jurisdiction in the District Court and error in the final decree.

We agree with the Court below that the removal was proper. The principal defendant was incorporated under the laws of the United States and that has been established as a ground of jurisdiction since Osborne v. Bank of the United States, 9 Wheat. 738. Pacific Railroad Removal Cases, 115 U.S. 1. Matter of Dunn, 212 U. S. 374. We shall say but a word in answer to the appellants' argument that a suit against such a corporation is not a suit arising under those laws within Section 24 of the Judicial Code of March 3, 1911, c. 231; 36 Stat. 1087. The contrary is established and the accepted doctrine is intelligible at least since it is part of the plaintiffs' case that the defendant bank existed and exists as an entity capable of committing the wrong alleged and of being sued. These facts depend upon the laws of the United States. Bankers Trust Co. v. Texas & Pacific Ry. Co., 241 U. S. 295, 306, 307. Texas & Pacific Ry. Co. v. Cody, 166 U. S. 606. See further Smith v. Kansas City Title & Trust Co., February 28, 1921. A more plausible objection is that by the Judicial Code, Section 24, sixteenth, except as therein excepted national banking associations for the purposes of suits against them are to be deemed citizens of the States in which they are respectively located. But we agree with the Court below that the reasons for localizing ordinary commercial banks do not apply to the Federal Reserve Banks created after the Judicial Code was enacted and that the phrase 'national banking associations' does not reach forward and include them. That phrase is used to describe the ordinary commercial banks whereas the others are systematically called 'Federal Reserve Banks'. We see no sufficient ground for supposing that Congress meant to open the questions that the other construction would raise.

On the merits we are of opinion that the Courts below went too far. The question at this stage is not what the plaintiffs may be able to prove, or what may be the reasonable interpretation of the defendants' acts, but whether the plaintiffs have shown a ground for relief if they can prove what they allege. We lay on one side as not necessary to our decision the question of the defendants' powers, and assuming that they act within them consider only whether the use that according to the bill they intend to make of them will infringe the plaintiffs' rights. The defendants say that the holder of a check has a right to present it to the bank upon which it was drawn for payment over the counter, and that however many checks he may hold he has the same right as to all of them and may present them all at once, whatever his motive or intent. They ask whether a mortgagee would be prevented from foreclosing because he acted from disinterested malevolence and not from a desire to get his money. But the word 'right' is one of the most deceptive of pitfalls; it is so easy to slip from a qualified meaning in the premise to an unqualified one in the conclusion. Most rights are qualified. A man has at least as absolute a right to give his own money as he has to demand money from a party that has made no promise to him; yet if he gives it to induce another to steal or murder the purpose of the act makes it a crime.

A bank that receives deposits to be drawn upon by check of course authorizes its depositors to draw checks against their accounts and holders of such checks to present them for payment. When we think of the ordinary case the right of the holder is so unimpeded that it seems to us absolute. But looked at from either side it cannot be so. The interests of business also are recognized as rights, protected against injury to a greater or less extent, and in case of conflict between the claims of business on the one side and of third persons on the other lines have to be drawn that limit both. A man has a right to give advice, but advice given for the sole purpose of injuring another's business and effective on a large scale, might create a cause of action. Banks as we know them could not exist if they could not rely upon averages and lend a large part of the money that they receive from their depositors on the assumption that not more than a certain fraction of it will be demanded on any one day. If without a word of falsehood but acting from what we have called disinterested malevolence a man by persuasion should organize and carry into effect a run upon a bank and ruin it, we cannot doubt that an action would lie. A similar result even if less complete in its effect is to be expected from the course that the defendants are alleged to intend, and to determine whether they are authorized to follow that course it is not enough to refer to the general right of a holder of checks to present them but it is necessary to consider whether the collection of checks and presenting them in a body for the purpose of breaking down the petitioner's business as now conducted is justified by the ulterior purpose in view.

If this were a case of competition in private business it would be hard to admit the justification of self interest considering the now current opinion as to public policy expressed in statutes and decisions. But this is not private business. The policy of the Federal Reserve Banks is governed by the policy of the United States with regard to them and to these relatively feeble competitors. We do not need aid from the debates upon the statute under which the Reserve Banks exist to assume that the United States did not intend by that statute to sanction this sort of warfare upon legitimate creations of the States.

Decree reversed.