# FEDERAL RESERVE BOARD

WASHINGTON

X-3208
September 24, 1921.

SUBJECT: Letters from Treasury Department Regarding Currency Operations of Federal Reserve Banks.

Dear Sir:

I am transmitting herewith, for your information and attention, copies of two letters received from the Under Secretary of the Treasury, both dated September 22, 1921. One of these letters relates to the withdrawal of Federal Reserve Bank Notes from circulation and points out the inconvenience to which the Treasury is subjected by reason of the withdrawal of Federal Reserve Bank Notes from circulation in amounts greatly exceeding the coinage of silver dollars. The other letter relates to the practice of some of the Federal Reserve Banks to forward to the Treasury for redemption all National Bank Notes received for redemption or deposit, whether fit or unfit.

The matters referred to in these letters will be brought up for further consideration at the conference beginning October 25th, but in the meanwhile the Board suggests that the Federal Reserve Banks, which are now performing the functions of sub-treasuries, do all in their power to comply with the views of Treasury officials.

Very truly yours,

Enclosures.

Governor.

GOVERNORS AND AGENTS - ALL F.R.BANKS.

COPY

X-3208a

TREASURY DEPARTMENT

Washington

September 22, 1921.

My dear Governor:

I think that there has in recent months been some tendency upon the part of the Federal Reserve Banks to hasten too much the withdrawal of Federal reserve bank notes from circulation. This has resulted in some disturbance to the Treasury's program for the printing and distribution of paper currency, and I am therefore calling the facts to your attention in order that appropriate action may be taken, wherever necessary, by the Federal Reserve Banks.

On February 1, 1921, there were deposited with the Treasurer of the United States as security for issues of Federal reserve bank notes $259,375,000 of Pittman Act certificates and $14,730,200 of United States bonds, a total of $274,105,200. On the same date there were $220,911,066 of Federal reserve bank notes in circulation and $5,027,334 in the Treasury, a total circulation stock of $225,938,400. On September 1, 1921, $193,875,000 of Pittman Act certificates and $14,480,200 of United States bonds, a total of $208,355,200 were deposited with the Treasurer of the United States to secure Federal reserve bank note circulation, and $119,172,892 Federal reserve bank notes were in circulation, while $2,593,508 were in the Treasury, a total of $121,766,400. From these figures it will be seen that during the period in question $65,500,000 of Pittman Act certificates were retired and $250,000 of United States bonds were withdrawn from deposit with the Treasurer, making a total decrease in securities deposited of $65,750,000; while, on the other hand, circulation of Federal reserve bank notes decreased $104,172,000, the difference between the authorized and the actual circulation on February 1st being $48,166,800 and on September 1st $86,588,800.

The Treasury's policy with respect to the retirement of Pittman Act certificates was announced in the letter to you under date of February 21st, on the occasion of the first deliveries into the general fund of standard silver dollars recoined under the terms of the Pittman Act, and has contemplated that retirements would be made at such rate as standard silver dollars are recoined and paid into the general fund, and at the further rate of $5,000,000 per month out of the general fund until the difference between the amount of certificates outstanding and the amount of circulation secured thereby should be eliminated. It will be noted that the amount of this difference on February 1st was $48,166,800 which includes a certain amount of bank notes secured by United States bonds. The exact amount is not material, but the important point to note is that the difference shows a great increase on the same basis, standing at $86,588,800 on September 1st, notwithstanding the monthly redemptions of $5,000,000 of certificates out of the general fund. As a matter of fact, the difference should have been decreased rather than increased in view of the amount of certificates thus redeemed - some $35,000,000.

The conclusion is inevitable that the circulation of Federal reserve bank notes is not being maintained. If, for example, the actual circulation had been maintained, except as diminished from time to time through payment into the general fund of standard silver dollars coined and the retirement of an equal par amount of certificates, the amount of bank notes outstanding on September 1st would have been something over $190,000,000 instead of some $120,000,000.

The understanding reached at the April conference of Governors of the Federal Reserve Banks, and approved, as I understand it, by the Federal Reserve Board, was that so far as possible Federal reserve bank notes would be continued in circulation pending replacement by silver certificates issued against standard silver dollars recoined pursuant to the operation of the Pittman Act, retirements of bank notes to keep pace with new issues of silver certificates. At the present time, however, bank notes are being retired several times as fast as new silver certificates are being issued. I wish, therefore, that you would cause the whole situation to be investigated, with a view to determining the difficulty and correcting it so far as possible. It seems to me important from every point of view that the contraction in Federal reserve bank note circulation should not be so abrupt, if for no other reason than to avoid waste in printing. Federal reserve bank notes are available in reserve here at Washington and at Federal Reserve Banks in large amounts, (over $30,000,000 in 1's and $19,000,000 in 2's at Washington, and over $6,000,000 in 1's and $3,000,000 in 2's at the Federal Reserve Banks). The contraction of this form of currency, moreover, leads to additional demands upon the Treasurer to supply other kinds of currency in corresponding amounts where needed, and even now the Treasury is under great pressure to supply the necessary amounts of silver certificates and legal tender notes. Redemptions of Federal reserve bank notes have been quite disproportionate to new issues in recent months. For example, it is noted that during July, 1921, $12,616,000 Federal reserve bank notes of the $1 denomination were redeemed and only $3,220,000 were issued; during the following month, August, $13,416,000 were redeemed and only $2,300,000 issued.

I should be glad if you could consider at the same time one further matter connected with the currency supply. It is the policy of the Treasury Department to issue silver certificates for the most part in the denomination of $1, with occasional issues in denominations of $5 and over to use up accumulated stocks. In due course, however, after all standard silver dollars have been recoined and the Pittman Act certificates and the Federal reserve bank notes secured thereby retired, practically all the $1 notes in circulation will be silver certificates, to be supplemented, when and as necessary, by such issues of United States notes in the $1 denomination as may be required. This policy will require that payments be made in United States notes in denominations of $2, $5, $10 and $20. This situation exists to some extent even now, and I understand that some difficulty is being experienced with some Federal Reserve Banks who object to the acceptance of shipments of United States notes from the Treasury in the higher denominations. I think it should be definitely understood that the Federal Reserve Banks will be expected to receive United States notes even in the higher denominations for credit in the Treasurer's account or otherwise for Treasury account. United States notes are legal tender and under the law it is necessary to maintain in circulation some $346,000,000 aggregate amount. The only way in which this circulation can be maintained is through payments in acceptable denominations, and the acceptable denominations ultimately will not include the $1 denomination in any great amount. It will be necessary, therefore, for Federal Reserve Banks from time to time to accept United States notes in available denominations above $1 and to make payments therein on account of redemptions or for other accounts. Otherwise it will be necessary for the Treasury to discontinue the currency distribution system now in effect and to resort to actual payments on redemption and exchange accounts at the Treasury in Washington and perhaps other Treasury offices throughout the country.

I shall be glad to have your comments on the situation and to be advised of any corrective measures which may be taken.

Very truly yours,

(Signed) S. P. Gilbert, Jr.

Under Secretary.

Hon. W. P. G. Harding,

Governor, Federal Reserve Board.

COPY. THE UNDER SECRETARY OF THE TREASURY

Washington

X-3208b
September 22, 1921.

Dear Governor Harding:

There has been within the past few months a marked acceleration of redemptions of national bank notes, which is doubtless due in large part to the decreased demand for currency and the improved standards implied to the money in circulation. I am inclined to believe, however, that these circumstances do not fully account for the increased redemptions, and I am accordingly writing to ask if you could ascertain to what extent the change may be due to the policy which has been adopted by some of the Federal Reserve Banks of refusing to pay out national bank notes. Many of the Federal Reserve Banks, as, for example, the Federal Bank of New York, pay out in ordinary course all fit national bank notes received. Other Federal Reserve Banks, as for example, the Federal Reserve Bank of Richmond, and, I think, the Federal Reserve Bank of Dallas, forward to the Treasury for redemption all national bank notes received for redemption or on deposit, whether fit or unfit. This practice throws extra burdens on the National Bank Redemption Agency, increases the turnover of national bank notes, and occasionally results in the redemption of absolutely new national bank notes received by the Federal Reserve Banks for deposit. This lack of uniformity on the part of the Federal Reserve Banks in the matter of payments of national bank notes is of long standing, but it has become more important with the abolition of the sub-treasuries and the concentration of currency functions in the Federal Reserve Banks and branches. The question of the policy to be followedwas considered at some length at the April, 1921, conference of the Governors, but without reaching uniformity. A resolution was there adopted to the effect that while it was desirable that Federal Reserve Banks should receive for credit and redemption by the Treasury Department unfit national bank notes, the practice of receiving national bank notes on deposit should be left to the several Federal Reserve Banks. Some Federal Reserve Banks, as I understand it, took the position that to pay out national bank notes rather than their own Federal Reserve notes would involve some loss to the Federal Reserve Bank, though it has seemed to me difficult to demonstrate that in the present position of the Federal Reserve System there would be any loss involved.

It seems to me that the question of policy is of sufficient importance, both from the point of view of the Treasury and the point of view of the Federal Reserve System, to have consideration by the Federal Reserve Board, and perhaps that some investigation should be made by the Board into the existing situation. I should be glad to know the views of the Board in the matter, and the results of any investigation that may be made.

Very truly yours,

(Signed) S. P. GILBERT, JR.

Hon. W. P. G. Harding,
Governor, Federal Reserve Board.