

STATEMENT FOR THE PRESS

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Eligibility of Paper of Cooperative Marketing Associations for purchase or rediscount by Federal Reserve Banks.

The Federal Reserve Board announced today an amendment to its Regulation B which makes eligible for purchase by Federal Reserve Banks on the open market bankers' acceptances with maturities up to six months which are drawn by growers or by cooperative marketing associations to finance the orderly marketing of non-perishable, readily marketable, staple agricultural products when secured by warehouse receipts covering such products.

This amendment to the Board's Regulation should be of material assistance to cooperative marketing associations in financing the orderly marketing of such agricultural products, and it is in line with the Board's policy of being as liberal as possible under the terms of existing law and in ruling on the eligibility of the paper of cooperative marketing associations for purchase or rediscount by Federal Reserve Banks.

That the Federal Reserve Board is greatly interested in the cooperative marketing movement and has sought every opportunity to assist the organizers and managers of such associations

to work out the best means of arranging their financing so that it should not only be sound but should also enable them to obtain the lowest interest rates for necessary credit as indicated by the number of very liberal rulings on this subject which the Board has issued during the past eighteen months.

These rulings, having reference to what is called the "eligibility" of notes and drafts for rediscount, were made from time to time as questions were submitted from various sections of the country. They involved farm produce differing as widely as fruit from California, wheat from the middle west and tobacco and cotton from the South, but the same principles of sound financing were involved in all, and in each case the cooperative association was a non-stock, non-profit corporation, the members of which consisted exclusively of growers of the particular crop which the association was organized to market. The growers agreed to sell and deliver their entire crops to the association, title passing at the time of delivery, and the association assuming absolute control over the commodities and their re-sale. Generally speaking, the commodities were pooled according to grades and after all of a particular pool had been sold the proceeds were distributed pro rata. It should be understood that the Board's ruling on this subject would not necessarily apply to associations operating on a materially different plan.

Several kinds of borrowings are involved. If the grower desires to do the borrowing himself he can draw a draft

on the cooperative association at the time he delivers his crop, the association accepting it. He then discounts the draft at his local bank, which under the Board's ruling may rediscount it at a Federal Reserve Bank as agricultural paper with a maturity up to six months. If the association itself wishes to borrow directly from a bank in order to make payments to the growers who are its members, its notes are eligible for for rediscount but the Board has held that under existing law such notes are commercial notes the maturity of which must not exceed ninety days, because the proceeds of such notes are used for the commercial purpose of buying the commodities from the growers. A bill now pending in Congress would make such notes eligible as agricultural paper with maturities up to nine months.

There was considerable discussion over the first mentioned case, where the grower draws his own draft on the association, as to whether the draft should be considered agricultural and have a six months' maturity. The law says the proceeds must be used for an agricultural purpose, and the point was made that the grower in all probability would use the money so obtained in paying debts previously incurred. It was suggested that unless this could be held to be an agricultural purpose, little agricultural, or six months, credit could be obtained in this way. In replying to this suggestion, the Federal Reserve Board ruled that when a farmer or grower delivers his crop to

a cooperative marketing association actually engaged in orderly marketing and when he is obliged to borrow money for ordinary general purposes, such as the payment of obligations previously incurred in growing or harvesting the same crop, a draft drawn by him on the marketing association for a part of the market value of the crop may properly be considered as drawn for an agricultural purpose.

This ruling has rightly been regarded as a very liberal one, and will greatly facilitate the operations of cooperative associations - in fact has already done so. It is based upon the principle, long recognized by the Board, that the carrying of agricultural products for such periods as are reasonably necessary in order to accomplish orderly marketing is a legitimate and necessary step incident to normal distribution. The Board pointed out, however, that there is a distinction between carrying products for such periods as are reasonably necessary and mere speculative withholding from the market in the hope of obtaining higher prices. Under the Federal Reserve Act paper drawn to finance speculation is ineligible for rediscount. The Federal Reserve Board also pointed out that in determining whether or not an association is engaged in orderly marketing, rather than speculative holding, it is not improper to take into consideration the fact that each crop must ordinarily support the market until the next crop is harvested.

A further and material aid to cooperative marketing associations is the ruling that bankers' acceptances drawn to finance the domestic storage of commodities pending orderly marketing by such associations are eligible for rediscount. In creating such acceptances the association arranges for a credit with some national or State bank which accepts its drafts to the amount arranged for when covered by warehouse receipts, and after acceptance such drafts are eligible for rediscount or for purchase in open market by Federal Reserve Banks. Under existing law, they are eligible for rediscount only when they have not more than three months to run. Heretofore, they have been eligible for purchase by Federal Reserve Banks only when their maturities at the time of purchase did not exceed three months; but the new amendment to the Board's regulation permits them to be purchased with maturities up to six months. Bankers' acceptances are recognized as the most desirable form of credit, as they sell on the credit of the accepting bank as well as on their backing of staple collateral and they usually take the lowest rate of interest, if properly drawn and safeguarded.

One of the most recent, and also one of the most liberal, rulings of the Board on this subject was to the effect that where a member of a cooperative association delivers his crop to the association and at substantially the same time draws a draft on the association which is accepted by it and discounted by the drawer at his own bank, such a draft is a "bill of exchange

drawn in good faith against actually existing values" and, therefore, is not subject to the 10% limitation prescribed in the Federal Reserve Act on the aggregate amount of paper of any one borrower which a Federal Reserve Bank may rediscount for any one member bank. This should be very beneficial to the farmers and their associations because it permits the rediscount of such paper in unlimited amounts.

The above are not all of the rulings made by the Federal Reserve Board on this subject, and, of course, there are other classes of eligible paper that can be used in borrowing by cooperative marketing associations, but they are probably the most important rulings. It should be understood also that the above statements are not intended as precise technical statements. All of the Board's various rulings on this subject except the one last mentioned were brought together and summarized in the Federal Reserve Bulletin for September, 1922 (page 1044 of the large edition and page 269 of the first edition) to which reference should be made by managers of associations, bankers and others interested in exact statements and in the legal points involved.