

C O P Y

FEDERAL RESERVE BANK

OF CLEVELAND

X-4032

April 18, 1924.

Mr. Walter Wyatt,
General Counsel,
Federal Reserve Board,
Washington, D. C.

Dear Mr. Wyatt:

I acknowledge receipt of your letter of April 15, enclosing revised draft of Regulation J, which you submitted to the Federal Reserve Board.

I note that you have incorporated some further changes and these appear to me to meet some of the objections. There is, however, one portion of Section 5 which I believe still needs revision and I notice that you have not adopted a change which we recommended in connection with this section. Paragraph 4, Section 5, reads as follows:

"Checks received by a Federal Reserve Bank on its member or non-member clearing banks will ordinarily be forwarded or presented direct to such banks and such banks will be required to remit or pay therefor at par in cash or bank draft acceptable to the collecting Federal Reserve Bank, or at the option of such Federal Reserve Bank to authorize such Federal Reserve Bank to charge their reserve accounts or clearing accounts."

The language of the last portion of this paragraph seems to me to be needlessly involved. Furthermore, it raises a question as to the legal right of a Federal Reserve Bank to charge the reserve account of a member bank or the clearing account of a non-member clearing bank, in the event that such member or non-member clearing bank fails to authorize the Federal Reserve Bank to do so. I think I understand the objections which may have been raised by some of the Federal Reserve Banks to the language which you have stricken out in the revised regulation. In striking it out, however, you may have met the objections of some of the Federal Reserve Banks but a new objection was raised from the standpoint of those Reserve Banks which may feel that they desire to reserve the right to charge the reserve account of the member bank or the clearing account of a non-member bank in case of the failure of a member or non-member clearing bank after checks sent to them for collection have been charged to the customers' account but before a remittance in acceptable funds has been received by a Federal Reserve Bank.

The language of the revised regulation, I think you will agree,

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specifically gives the Federal Reserve Bank the right to charge the reserve account or the clearing account only when authorized by the member bank or the non-member clearing bank to do so. Inasmuch as the language is specific, it would seem that the courts might hold that Federal Reserve Banks had the right to charge the reserve account or clearing account only when authorized to do so and it might be presumed by the courts that the Federal Reserve Banks were prohibited from exercising this right in the absence of specific authorization from the member or non-member clearing bank.

In our district, we require our member banks (and we have no non-member clearing accounts outside of Cleveland) to remit for the checks which we send to them. In some cases, we permit them to authorize us to charge their reserve account but we specifically reserve the right in our check collection circular to charge the reserve account whenever in our judgment we deem it necessary to do so. This reservation is for our protection in the case of the failure of a member bank and we have found it very useful in several cases recently, notably in the cases of the Springfield National Bank and the National Bank of Barnesville, both of Ohio.

In either of these cases, had the receiver questioned our right to charge the reserve account under the terms of the revised Regulation J, I am inclined to think the court would have sustained the receiver for reasons given above. I would like, very much, to see incorporated in the new regulation, either the language which has been stricken out in the revised copy or the language suggested in my telegram of April 7th, as follows:

"Provided that the Federal Reserve Bank may effect payment of such checks by charging the reserve or clearing accounts of the drawee banks with them."

Those Reserve Banks which may object to this provision on the basis of court decisions giving the proceeds of checks handled for collection and remittance, a different status from the proceeds of checks sent for collection and credit, might object to either of these suggested changes. It occurs to me, however, that their objections might be overcome, if the following were substituted:

"Provided, however, that the Federal Reserve Bank will retain all of its legal rights to protect itself in cases of emergency."

Very truly yours,

(Signed) H. F. Strater,
Assistant Cashier.