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FEDERAL RESERVE BANK
OF RICHMOND

X-4642

July 26, 1926.

Federal Reserve Board,
Washington, D.C.

Attention of Mr. Walter Wyatt, General Counsel.

My dear Mr. Wyatt:

At the recent trial of the case of Craven Chemical Company v. Federal Reserve Bank of Richmond and Cleve & White, the District Court of the United States for the Eastern District of North Carolina instructed a verdict in favor of the Federal Reserve Bank of Richmond and against Cleve and White.

The facts of this case were as follows: Cleve and White drew a check on the Bank of Vanceboro in favor of the Craven Chemical Company. The check was deposited by the Craven Chemical Company in the Murchison National Bank of Wilmington under a deposit slip which made that bank a forwarding agent. The Murchison National Bank sent the check to the Federal Reserve Bank of Richmond for collection in accordance with the terms of its circular. The Federal Reserve Bank of Richmond sent the check to the Bank of Vanceboro on which it was drawn for remittance. The last mentioned bank sent a draft for the amount of this check and other checks sent to it at the same time, which draft was drawn upon the National Bank of New Bern, a designated reserve depository of the Bank of Vanceboro. The draft was promptly presented, but was dishonored, and the Bank of Vanceboro failed. The Craven Chemical Company instituted an action against the Federal Reserve Bank of Richmond and Cleve and White, alleging that the Federal Reserve Bank was negligent, and also alleging in the alternative that Cleve and White had not been released from liability upon the original check given by them.

The suit was instituted in the State Courts of North Carolina, but removed to a Federal Court before the passage of the Act of Congress depriving Federal Courts of jurisdiction of actions against Federal Reserve Banks. After several continuances the case was recently tried. The Court, as I say, instructed a verdict in favor of the Federal Reserve Bank of Richmond and against Cleve and White. We, of course, had pleaded and proved the sending of our circular concerning our liability for checks received for collection to the Murchison National Bank. We also relied upon Chapter 20 of the Public Laws of North Carolina for 1921, commonly called the Anti-par Clearance Act, which authorizes a State bank to pay a check presented by a Federal Reserve Bank by means of an exchange draft.

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There was no formal opinion but Judge Meekins in announcing his intention to instruct a verdict in our favor stated that the last mentioned statute of North Carolina certainly operated to relieve a Federal Reserve Bank of any liability upon the ground that it accepted an exchange draft in settlement.

Judge Meekins also held that under the terms of this statute the drawer of the check was not released. Prior to the statute a check was an unconditional order for legal tender money, and the drawer engaged that it would be paid according to its tenor - that is to say in legal tender money. If the holder elected not to demand lawful money, but to accept a substituted medium of payment such as an exchange draft, the holder failed to fulfill the condition upon which he could have recourse to the drawer, so that the drawer was released, and the check paid as to the drawer, but under the North Carolina Statute the holder is presumed to have given an order payable by money, or by an exchange draft; consequently he engages that the check will be paid according to its tenor - that is to say by means of lawful money or a collectible exchange draft, and if a worthless exchange draft be given by the drawee bank the drawer is still bound upon his engagement because the holder has demanded payment of the check according to its tenor, but has not received it.

You will readily see this decision is of no especial interest, except in North Carolina, and in those States, if any, which have similar Acts.

The points decided by the trial judge appear to me to have been already decided by the Supreme Court of North Carolina in *Federal Land Bank v. Barrow*, 127, S. C. p. 3, and in *Graham v. Proctorsville Warehouse*, 127 S.C. p. 540.

The Judge stated to me informally that had the North Carolina statute not been in force, he would have still been inclined to give judgment in favor of the Federal Reserve Bank upon the authority of *Fergus County v. Federal Reserve Bank of Minneapolis*, 244 Pac. 883; but as you can see from the above discussion it was unnecessary for him to consider the application of the uniform check collection circular in view of the fact that he held that the North Carolina Statute was of itself a sufficient defense to any action against the Federal Reserve Bank.

In the course of the trial, an interesting question was raised as to whether or not knowledge by the Federal Reserve Bank of the weakened condition of the Bank of Vanceboro was material. We contended that as long as the bank was open for business, we could not refuse an exchange draft, and that, therefore, our knowledge or ignorance of its condition was immaterial. The Judge at first admitted evidence showing that the Bank of Vanceboro had been for sometime in a weakened condition, but later struck out this testimony upon the ground that the plaintiffs had failed to show that we had any knowledge of this condition, or could have obtained such

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knowledge by the exercise of ordinary diligence.

The opposing Counsel have informally notified me that they would appeal from the decision of the trial court, but no formal steps have as yet been taken.

With best personal regards, I remain

Very truly yours,

(Signed)

M. G. Wallace,
Counsel.

MGW:IB