

FEDERAL RESERVE BOARD

WASHINGTON

X-4971

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

October 14, 1927.

SUBJECT: Deductions in Computing Reserves of Member Banks.

Dear Sir:

Pursuant to the action taken by the last Governors' Conference the Federal Reserve Board has given careful reconsideration to its ruling contained in the last paragraph of the Board's letter of March 24, 1927, (X-4816). In this ruling, which had to do with items such as coupons, checks drawn on themselves by corporations other than banks, bill of lading drafts, etc., it was held that where there is an agreement between the forwarding bank and the correspondent bank by the terms of which credit is given to the forwarding bank immediately upon receipt by the correspondent, items of this kind may be deducted from due to bank balances by the forwarding bank in computing its reserves as soon as these items have been placed in the mails and charged to the account of the correspondent bank, regardless of whether or not the forwarding bank has given credit to its own depositor.

The last Governors' Conference took the position that this ruling would have the effect, if generally adopted as a practice by member banks, "of reducing very considerably the liability in the item 'due to banks', upon which the reserve calculation is made, which appears to be unjustifiable."

The question whether certain items should be considered as amounts "due from" banks is separate and distinct from the question whether such items constitute deposit liabilities against which reserves should be maintained. The two questions are independent and the answer to one of them does not necessarily depend upon the determination of the other. For instance, items received by the forwarding bank in payment of debts due it or items otherwise actually owned by the forwarding bank are deductible from "due to" bank balances when forwarded for collection and charged to the account of the correspondent bank, notwithstanding that there is no corresponding deposit liability. The right to deduct amounts from balances due to banks does not depend under the law, on whether or not there is a corresponding deposit liability but on whether the amounts proposed to be deducted may properly be considered "due from other banks."

In the Board's ruling on this subject of March 24, 1927, (X-4816) the question under consideration was whether items of the kind described might be deducted as "due from bank balances" where there was an agreement by the correspondent bank to give immediate credit to the forwarding bank for such items. In the Board's opinion as set forth in that ruling, when there is an agreement between the forwarding bank and the correspondent bank by the terms of which credit is given to the forwarding

bank immediately upon receipt by the correspondent, such non-cash items when placed in the mails and charged to the account of the correspondent bank may be deducted by the forwarding bank in computing its reserves, regardless of whether or not the forwarding bank has given credit to its own depositor. In the absence of such an agreement the deduction may not be made until the items have actually been collected and placed to the credit of the forwarding bank.

Upon consideration of the other phase of this matter, it is the Board's opinion that when there is an agreement by the correspondent bank to give credit to a forwarding bank immediately upon receipt, items such as coupons, checks drawn on themselves by corporations other than banks, bill of lading drafts, etc., which have been placed in the mails and charged to the account of the correspondent bank in accordance with the existing agreement, should be considered deposit liabilities of the forwarding bank against which reserves should be computed. Where items of this kind are forwarded by a bank to its correspondent under an agreement for immediate credit by the latter, they are in effect being treated as checks or other cash items. Cash items, however, while deductible as "due from bank balances" when placed in the mails and charged to the account of the correspondent bank, also constitute deposit liabilities against which reserves should be maintained by the forwarding bank. Accordingly, such non-cash items should, when the conditions described exist, be included in deposit liabilities against which reserves must be maintained.

By direction of the Federal Reserve Board.

Walter L. Eddy,
S e c r e t a r y.

TO ALL CHAIRMEN AND GOVERNORS
OF F. R. BANKS.