X-9623

INTERPRETATION

BANKING ACT OF 1935

(Copies to be sent to all Federal reserve banks)

June 17, 1936.

Honorable J. F. T. O'Connor,
Comptroller of the Currency,
Washington, D. C.

Dear Mr. O'Connor:

This refers to Deputy Comptroller Lyons' letter of May 19, 1936, inquiring whether the discount with a national bank of commercial paper held by a hardware company which is solely owned by the president of the bank and indorsed by such company "without recourse" is to be considered a violation of Regulation O or an attempt to evade the provisions thereof. It is understood that the president of the bank is engaged in the hardware business under a trade name and that such business is not incorporated. It appears that you have previously advised the president that the unqualified indorsement in the trade name of the hardware company of paper held by it and discounted with the bank was considered the equivalent of the indorsement of the president of the bank, thereby bringing him within the prohibitions of Regulation O and that, following such advice, the hardware company continued to discount with the bank notes owned by the hardware company which it had received for merchandise sold but now indorses such paper "without recourse".

Section 1(c) of Regulation O defines the terms "loan", "loaning", "extension of credit", and "extend credit" as including, among other things, the acquisition by discount, purchase, exchange, or otherwise of any note, draft, bill of exchange, or other evidence of indebtedness upon which an executive officer of a member bank may be liable "as maker,

drawer, indorser, guarantor, or surety", and it is further provided that such terms shall include any other transaction as a result of which an executive officer becomes obligated to a bank directly or indirectly by any means whatsoever, "by reason of an indorsement on an obligation or otherwise, to pay money or its equivalent". Under the usual rules of law an indorsement "without recourse" constitutes the indorser as the mere assignor of title to the instrument and such an indorsement is designed to protect the indorser from liability on the instrument. In the circumstances, it is the Board's view that where an executive officer merely indorses a note to his bank "without recourse" and does not become liable to the bank on such instrument, the transaction does not fall within the provisions of section 22(g) or of Regulation O.

While it might appear from the facts submitted that an indorsement "without recourse" by the hardware company is an attempted evasion of the law, the fact remains that the transaction described is not now covered either by the terms of section 22(g) or the Board's Regulation O and it is doubtful whether cases of this kind are of sufficient importance or will arise with sufficient frequency to justify an amendment to the Board's regulation. If, however, you feel that the continued acceptance by the bank of the notes of the hardware company indorsed "without recourse" is an unsafe or unsound practice, you might wish to consider proceeding against the president of the bank under the provisions of section 30 of the Banking Act of 1933. Furthermore, since the president of the national bank is required under the law also to be a director thereof, it is assumed that, if you have not already done so, you will determine

whether the transactions conform to the requirements contained in section 22(d) of the Federal Reserve Act, relating to transactions between a member bank and its directors.

Very truly yours,

(Signed) L. P. Bethea

L. P. Bethea,
Assistant Secretary.