"The History and Development
of
The Federal Reserve System"

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A thesis submitted in partial fulfillment of the requirements for the degree of Bachelor of Science in the School of Commerce and Administration at Washington and Lee University.

June 1949.

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Chapter I.

Purpose Of The Federal Reserve System

On December 23,1913 President Woodrow Wilson signed the Federal Reserve Act establishing the Federal Reserve System. The Act was the climax of a quarter century of educational effort for the reformation of the banking system which began during the depression in 1893.(1) The founders of the Act studied not only American principles and practices, but also those of European countries in an effort to remove the defects of the national banking system.

The purposes of the founders of the Federal Reserve Act were several. According to the title of the Act,their purposes were to provide for the establishment of Federal Reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, and to establish a more effective supervision of banking in the United States.(2) The Act was designed to reduce the defects of the

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(1) Clark,Lawrence E.,Central Banking Under The Federal Reserve System,The Macmillian Company,New York,1935. p.32.

(2) Ibid,p.34.

national banking system from our economic life, and as a constructive measure it was designed to establish an institution to carry on the function of central banking. The institution which it set up was not a central bank but it was a central banking system. Over the years the system has developed a broader objective namely to help prevent inflation and deflation and to give aid in conditions of employment and a rising level of income.(3) The broader objective was well stated by President Roosevelt when he dedicated the Federal Reserve Building in Washington,D.C., in 1937: " I dedicate this building to progress toward the ideal of an America in which every worker will be able to provide his family at all times with an ever-rising standard of comfort."(4) It is to this ideal that the Federal Reserve System is dedicated.

The principal duties of the Federal Reserve include regulation of the money supply and also the maintenance of

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(3) Board of Governors of the Federal Reserve System, The Federal Reserve System-Its Purposes and Functions, The National PublishingCompany, Washington, D.C., 1947. p.1.

(4) Ibid, p.1.

regular services for the member banks of the Federal Reserve System. These services include the following: "holding member bank reserve balances;furnishing currency for circulation;effecting telegraphic transfers of funds; faciliating the clearance and collection of checks; examining and supervising state member banks and obtaining reports of conditions from them;collecting and interpreting economic information bearing on credit problems; and acting as fiscal agents,custodians,and depositories for the Treasury and other governmental agencies."(5)

The regulation of the money supply, being the chief function of the Federal Reserve should be discussed in a manner showing what constitutes the money supply,and also by what means the Federal Reserve System may regulate this supply. The money supply consists of all kinds of money in circulation, both paper and coin, and also deposits held by the banks for their depositors. Bank deposits and currency serve the same general purpose,and can be

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(5) Ibid, p.5.

converted into each other at anytime.[6] Most people find it much more convenient to keep most of their money in banks, and therefore, bank deposits greatly exceed the amount of currency. "Because deposits and currency are closely related to loans and investments of banks,the term volume of bank credit and money supply generally mean the same thing,namely,the means of payment owned by the people of the country."[7]

The Federal Reserve System has a great influence on the money supply of our economy. Practically all of the money that is available for our use comes, directly or indirectly, through the banks. "Therefore,the supply of money in the country depends almost entirely on the ability of banks to meet the monetary requirements of industry,trade,agriculture, and other sectors of economic life. The ability of banks to meet the money needs of the

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(6) Ibid, p. 5.

(7) Ibid, p. 6.

people depends in turn on the amount of reserves they hold. This amount is affected by Federal Reserve operations." (8) Banks are allowed to lend and invest money only in proportion to the reserves at their disposal. "Thus, the Federal Reserve, through the determination of the cost and other conditions on which banks can obtain additional reserves, can influence the amount of money that they may pass on to the public through loans and investments.It is in this manner that the Federal Reserve System has power to influence the country's money supply." (9)

In an economy like ours, where practically all transactions are settled in money,regulation of the money supply gives the Federal Reserve great powers and places on its management a grave responsibility. The Federal Reserve alone cannot assure the maintenance of satisfactory economic conditions. These depend, in addition to the supply of money,on the demand for it, over which the Federal Reserve can exert only an indirect and limited influence. There are a great

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(8) Ibid, p.9.

(9) Ibid, p.9.

Variety of other things on which they also depend, "including governmental policies in regard to expenditures, taxes,and debt; the distribution of income among different groups of the population; the bargaining strength and policies of management and labor and of agricultural and other sectors of the economy;the power of monopolies; the course of foreign trade and foreign investment; and the prospects for peace."(10)

The Federal Reserve Act does not destroy our American system of small independent banks. The law includes these thousands of independent banks with all their essential functions, and joins them into a unified system which is democratic in its organization and nationwide in its field of operation- a system dedicated to public service.(11)

"To meet the heavy responsibilities placed upon the Federal Reserve System,two things are absolutely

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(10) Ibid,p.9.

(11) Kemmerer,E.W., The A.B.C. of The Federal Reserve System,Princeton University,Press, Princeton, New Jersey, 1919, p.28

essential--good management, and ample powers and resources. Good management cannot be secured with certainty by means of legislative provisions, however carefully designed with that end in view." (12) Under the Federal Reserve Act, an ingenious combination of government and banking influence is provided in selecting the management. Purely banking operations are largely to be handled by boards of directors of directors of which a majority of the membership is to be chosen by banks. General supervision, and for some purposes control, is placed with the Federal Reserve Board which is to be appointed by the President of the United States, and with the advise and consent of the senate. (13) The Federal Reserve Banks have public interest as the purpose of operation and are not influenced by private gain. Although the Reserve Banks pay legally prescribed dividends on their capital stock, the making of profits is not the purpose of their existence nor the basis for determining the character of their operations. (14)

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(12) Phillips, Chester A., Readings In Money and Banking The Macmillan Co., New York, 1920, p.723.

(13) Ibid, p.724.

(14) Banking Studies, Member of the Staff Board of Governors of the Federal Reserve System, Waverly Press, Inc. 1941 p.231.

Chapter II

Structure of Federal Reserve System

By the end of 1946 the Federal Reserve System had a total of 6900 member banks. Membership in the Federal Reserve System consists of all national banks, which are required to belong, or give up their national charters, and all state banks that are eligible and who voluntarily chose to belong. At the end of 1946 less than 50% of all banks in the country were members of the Federal Reserve System, hoever, they held over seventy-five per cent of the total deposits of all banks.(1)

Member and non member banks in individual states vary to a great extent. In the Eastern states,particularly in the Northeastern States, membership in the Federal Reserve System is high, consisting of about three fourths of the banks. However, in most of the Middle Western and Southern States, the number of non-member banks usually greatly exceeds the number of member banks. The deposits

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(1) Board of Governors of the Federal Reserve System, The Federal Reserve System- Its Purposes and Functions, The National Publishing Company,Washington,D.C.,1947 p.48.

of member banks in all states, except Mississippi, greatly exceed the deposits of nonmember banks.(2)

For purpose of administering the Federal Reserve System, the country is divided into twelve districts with a Federal Reserve Bank located in each district. "In determining the boundaries of these districts, the authorities were required to have regard to the convenience and customary course of business, to make each district large enough to provide the minimum capital of $4,000,000 required by law, and to make none so large as to dominate the others thereby endangering the Federal principle which the law sought to establish."(3) The boundaries of the various districts do not necessarily follow state lines and in many cases states are divided into more than one district. Although the country has been divided into twelve districts, the Federal Reserve Act gives leeway in that

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(2) Board of Governors of the Federal Reserve System, Banking Studies, Waverly Press, Inc., Baltimore, 1941. p.92.

(3) Kemmerer, E.W., The A.B.C. of the Federal Reserve System, Princeton University Press, Princeton, N.J., 1919, p.28-29.

it calls for the country to be divided into not less than eight, nor more than twelve districts.(4) The law also requires that there be a Federal Reserve Bank in each district, and some also gives authority for Reserve Banks to have branch banks. The following is a list consisting of the various districts and branches throughout the country:

District Number 1.-------- Federal Reserve Bank of Boston

District Number 2.-------- Federal Reserve Bank of New York. Branch at Buffalo, New York.

District Number 3.-------- Federal Reserve Bank of Philadelphia

District Number 4.-------- Federal Reserve Bank of Cleveland. Branches at Cincinnati, Ohio and Pittsburgh, Penna.

District Number 5.-------- Federal Reserve Bank of Richmond. Branches at Baltimore, Maryland and Charlotte, North Carolina. (5)

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(4) Phillips, Readings In Money and Banking, The Macmillan Company, 1920, p. 724.

(5) Board of Governors of Federal Reserve System, Its Purposes and Functions, Op. Cit. p. 51.

District Number 6.---------Federal Reserve Bank at Atlanta. Branches at Birmingham,Alabama; Jacksonville,Florida;Nashville, Tennessee; New Orleans,Louisiana

District Number 7.---------Federal Reserve Bank of Chicago Branch at Detroit, Michigan.

District Number 8.---------Federal Reserve Bank of St.Louis. Branches at Little Rock,Arkansas; Louisville,Kentucky,Memphis,Tennessee.

District Number 9.---------Federal Reserve Bank of Minneapolis.Branch at Helena,Montana.

District Number 10---------Federal Reserve Bank of Kansas City.Branches at Denver,Colorado; Oklahoma City,Oklahoma;Omaha, Nebraska.

District Number 11---------Federal Reserve Bank of Dallas, Branches at El Paso,Texas; Houston,Texas; and San Antonio, Texas. (6)

District Number 12---------Federal Reserve Bank of San Francisco. Branches at Los Angeles, California;Portland, Oregon; Salt Lake City,Utah; Seattle,Washington. (7)

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(6) Ibid, p.53.

(7) Ibid, p.53.

Each Federal Reserve Bank is a corporation organized to benefit public service. The main difference between the Federal Reserve Banks and privately managed banks is that profits are not the main objective of their operations, and stockholders, who are the member banks of each district, do not have the same priviledge of similar privately managed corporations.

Like most corporations, each Federal Reserve Bank is governed by a board of directors- in this case a board of nine directors is divided evenly into three classes, known as Class A directors,Class B directors and Class C directors. Class A directors are usually chosen from the ranks of bankers.[8] Class B directors are usually actively engaged in the district in commerce,agriculture or industry, and must not be officers, directors or employees of any bank. The three Class C directors are not elected by the member banks, but are appointed to the board by the Board of Governors.[9] Since two thirds of

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(8) Foster and Rodgers, Money and Banking,Third Edition, Prentice-Hall,Inc., New York,1947,p332.

(9) Ibid, p.332.

the bank's directors are chosen by member banks, the banking interests are left in control of each Federal Reserve Bank.

Because Federal Reserve Banks are not intended to be profit making institutions, the stockholders receive dividends only after all necessary expenses have been paid. They are allowed a cumulative dividend of 6 per cent per annum. Any remaining profits are credited to surplus of the Federal Reserve Bank under the provision of the Banking Act of 1933.(10)

The banks in the Federal Reserve System that have direct relations with the public are the member banks. As stated before, these fall into two classes: the national banks which are compelled to join under the law, and state banks which may become members by choice. If any national bank failed to subscribe for its share of the capital stock of the Federal Reserve Bank of its district it was forced to give up its charter as a national bank.(11) State Banks

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(10) Ibid, p. 333.

(11) Froman, Lewis A., Principles of Economics, Revised Edition, 1946, Richard D. Irwin, Inc., Chicago, Illinois. p. 620-621

to qualify for membership, needed to comply with certain conditions imposed upon national banks, including minimum capital requirements for cities of a given size, legal reserves must be maintained in the form of a deposit with the Federal Reserve Bank of its district, limitations placed on loans, and accept examination made by the Federal Reserve Banks. Also, membership for state banks requires that a bank subscribe to the capital stock of the Federal Reserve Bank of its district to the extent of 6 per cent of its capital.(12)

The principal functions of the Federal Reserve Banks are separated into four groups: (1) rediscounting; (2) open market operations; (3) note issue; and (4) clearings and collections.(13)

Rediscounting of commercial paper by the Federal Reserve Bank is one of the means that member banks can obtain and keep its credit. When a member bank makes a loan to one of its customers, usually in the form of a promissory note, they serve as the assets of the commercial bank.(14)

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(12) Ibid, p.621.

(13) Ibid, p.624.

(14) Ibid, p.625.

The member bank may then take the promissory note to the Federal Reserve Bank of its district and have it rediscounted. The Federal Reserve Banks provide an organized market for rediscounts of which member banks, during emergency conditions may avail themselves. When a member banks seeks this rediscounting function of the Federal Reserve Bank, it is not assured that the loan will be made.(15) The Federal Reserve Bank is under no obligation to grant the credit, but its decision is weighed on its judgment concerning the member bank's needs and the use to be made of the additional funds.

Any member bank in good standing and with sufficient collateral can usually receive these benefits from the Federal Reserve Bank. The principal determinate of whether loans will be made is set not in the granting and refusing of loans, but in the prevailing rate of rediscount.(16) As a general rule, if business is fairly normal, an increase

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(15) Board of Governors, Federal Reserve System, Its Purpose and Functions, Op.Cit.p.25.

(16) Ibid, p.26.

in the rediscount rate, which must be passed on to bank customers, tends to discourage additional borrowing and thus to prevent large expansion of loans. Similarly, under normal business conditions, a decrease in the rate of rediscount may encourage new borrowing and stimulate an expansion of loans. It is chiefly in this way that the Federal Reserve System expresses its policy with respect to the money supply of the country.(17)

The second main function of the Federal Reserve Bank is engaging in open market operations. These open market operations differ from rediscounting operations in that the initiative is taken by the Federal Reserve, and not by the member banks.(18) An open market is free to anyone who wishes to buy or sell and thus there are no restrictions to members. When Federal Reserve Banks buy obligations and securities in the open market they are supplying the market with funds and thus helping to ease the money market.(19)

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(17) Ibid, p.26-27

(18) Ibid, p.27

(19) Foster and Rodgers, Op.Cit. p.336.

On the other hand, when they sell government obligations and securities in the open market they are withdrawing funds from the market making the money market more rigid. Whether a member bank will sell securities to The Federal Reserve Bank or borrow will depend on the difference between the rate that Reserve banks will buy and the rediscount rate. Also the needs of the individual bank. (20) By selling they have funds and the Federal Reserve Banks have added to their own investment in securities. Thus, supplying the market with funds has a tendency to lower interest and discount rates and to encourage borrowing. Thus lowering the rediscount rates and buying in the open market are the principal devices which the Reserve Banks can use for making credit easier, and raising the discount rate and selling in the open market are the methods of restricting credit. (21)

The third main operation of the Federal Reserve Banks is the function of note issue. As has been previously stated, one of the chief reasons for the development of the Federal Reserve System was because of the inelasticity in our currency.

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(20) Ibid, p.337

(21) Ibid, p.337.

Currency is said to be inelastic when it cannot readily be expanded or contracted in response to changing needs. The Federal Reserve System has provided elasticity of currency in the form of two types of note issue- Federal Reserve notes and Federal Reserve bank notes.(22) The power to issue the latter has been deprived of the Federal Reserve Banks in 1945.

These Federal Reserve notes constitute the largest single element in our currency, accounting for about 80% of our total money in circulation. The security behind the Federal Reserve note is that it is backed 100%. Of this backing 25% must be in gold and the remaining 75 % may be in the form of rediscounts, acceptances, and United States Securities.

The elasticity of the Federal Reserve notes is in the fact that they can be increased or decreased in proportion to the various levels and demands of business. When

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(22) Froman, Lewis, A., Op. Cit. p.631.

(23) Ibid. p.631.

a member bank requires additional currency, it can obtain a supply from the Federal Reserve Bank, either by borrowing from the Federal Reserve Bank or by drawing on its surplus balances maintained by the Federal Reserve Bank. (24)

The fourth main functionof the Federal Reserve Banks is the clearing and collecting of checks. Checks which are drawn in the regular course of business are handled and collected through the Reserve Banks. Thus, if a manufacturer in Connecticut sells $1,000 worth of equipment to a dealer in California and receives a check on a bank in California, it can be handled through the channels of the Federal Reserve System. The Federal Reserve Act provides for a clearance system through the use of Gold Settlement Fund. (25) This fund, which is held in Washington, D.C., requires each Federal Reserve Bank to keep a deposit of gold certificates in the fund. At the end of each day, each Reserve Bank wires the administrator of the Gold Settlement Fund, the amount of cliams that it has against the other Reserve Banks. These claims are then offset by a bookkeeping transaction from

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(24) Foster and Rodgers, <u>Op.Cit</u>. p.333

(25) Froman, Lewis A., <u>Op.Cit</u>. p.634.

the account of one Reserve Bank to another. In this way, the Gold Settlement Fund serves as a national clearing house for the Federal Reserve Banks.(26) In the illustration cited above, the Connecticut manufacturer deposits the check on the California bank in his own bank. This Connecticut bank in turn sends it to the Federal Reserve District Bank in Boston. The Boston Reserve Bank in turn sends it to the Federal Reserve Bank in San Francisco and the Reserve Bank in San Francisco will present it to the bank upon which it is drawn. As soon as the California bank pays the Federal Reserve Bank of San Francisco, the Federal Reserve Bank of San Francisco in turn pays the Federal Reserve Bank of Boston through the medium of the Gold Settlement Fund.(27)

Checks which are collected and cleared through the Federal Reserve Banks must be paid in full by the banks on which they are drawn, without a deduction of a fee or charge. This is known as the par collection system and no bank charging a remittance fee against a Federal Reserve Bank can enjoy the privilege of this clearing system.(28)

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(26) _Ibid_, p.634.

(27) _Ibid_, p.634.

(28) _Ibid_, p.635.

Chapter III

Organization and Control of the Federal Reserve System

In order to appreciate the ways in which the Federal Reserve System serves the banking needs of the country, it is necessary to have at least an elementary understanding of the structure organization of that system. The five important agencies or parts of the system are the Board of Governors, the Federal Open Market Committee, the Federal Advisory council, and the Federal Reserve Bank and the member banks, which were discussed in a previous chapter.(1)

The Board of Governors of the Federal Reserve System is the coordinating and governing body of the entire system. It is a governmental institution and has its offices located in Washington, D.C.(2) The Board of Governors is composed of seven members, appointed by the President of the United States, with the advice and consent of the Senate.

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(1) Board of Governors of Federal Reserve System, The Federal Reserve System, Its Purposes and Functions. National Printing Company, Washington, D.C., p.56-58

The term of office is fourteen years, and the terms are so arranged that only one vacancy will normally occur every two years.[2] Members serving a full fourteen year term are not eligible for reappointment. Membership of the board is decentralized in that no two members of the Board may come from the same Federal Reserve district. One of the seven appointees of the President is designated as chairman and one as vice chairman to serve for four years. The salary arrived at for members of the Board of Governors is $15,000 a year.[3]

The principal duty of the Board of Governors is to supervise the workings of the Federal Reserve System. "In order to carry out their job, the Board has specific powers which are enumerated below:

(1) The approval of rediscount rate of each Federal Reserve Bank.

(2) To control open market operations."[4] Under the

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(2) Ibid, p.56.

(3) Bradford, F.A., Money and Banking, Longmans, Green and Co. Fourth Edition, 1937, p.410.

(4) Foster and Rodgers, Money and Banking, Third Edition Prentice-Hall, Inc., New York, 1947, p.328.

Banking Act of 1935, a Federal Open Market Committee was established which consisted of the seven members of the Board of Governors and five representatives of the Federal Reserve Banks.

"(3) To change Reserve Requirements. Board may change the requirements as to the reserves that member banks must maintain with the Reserve Banks.

(4) To approve the appointment of the president and first vice president of each Federal Reserve Bank.

(5) Determining and defining the character of the paper which is eligible for rediscount.

(6) To make examinations of the Reserve Banks, and to require reports of their conditions."[5]

(7) To supervise the issuance of Federal Reserve notes."[6]

In addition to the broad powers listed above, the Board of Governors has supervisory powers which include

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(5) *Ibid*, p.329

(6) *Ibid*, p. 330.

passing on applications for admission of new member banks, and permits to holding company affiliates to vote the stock of member banks. Also the Board issues regulations limiting the rate of interest which may be paid by member banks on deposits. (7)

As described in the above analysis, the Board carries on many kinds of work whichdiffer very widely from one another. They range between such extremes as determining the discount rate and requiring periodical reports on the conditions of the Reserve Banks. Because of the diversity of the work of the Board of Governors many unexpected problems of organization and management arise. In approaching these problems, the Board calls upon the assistance of its permanent staff and the various Federal Reserve Banks. (7)

Another of the important agencies of the Federal Reserve System is the Federal Open Market Committee. The

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(7) Board of Governors of the Federal Reserve System, Banking Studies, Waverly Press, Inc. 1941. p.370.

seven members of the Board of Governors together with five elected representatives of the Federal Reserve Banks constitute the Federal Open Market Committee. The representatives of the Federal Reserve Banks are selected by their boards of directors in the following manner:[8] One by the Boston and New York banks; one by the Philadelphia and Cleveland banks;one by the Chicago and St. Louis banks; one by the Richmond,Atlanta and Dallas banks; and one by the Kansas City,Minneapolis and San Francisco banks."[9]

It is the duty of the Federal Open Market Committee to decide when and how much to buy or sell in the open market and under what conditions. It is up to the Federal Reserve Banks as prescribed by law to follow out these decisions in any dealing in the open market. The Committee is aided in its work by a staff which is made up from the staffs of the Board of Governors and the Federal Reserve

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(8) Bradford,F.A., Op.Cit. p.410-411

(9) Ibid, p.411.

Banks. The Committee holds its meetings in Washington at least four times a year and more often if it is necessary and arrives at its policy through reviewing the business and credit conditions of the country as presented by its regional membership.(10)

The third agency in the organization structure of the Federal Reserve System and provided for in the Federal Reserve Act is the Federal Advisory Council.At the time of the establishment of the Federal Reserve System, the bankers wanted the Federal Reserve Board to consist of members selected by the banks.When this power was designated to the President, the law provided for an advisory body to be appointed by the Federal Reserve Banks themselves, one member from each of the banking districts into which the country is divided. The members are selected annually, by the board of directors of Reserve Bank. The council has no executive power,and acts

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(10) Board of Governors of the Federal Reserve System, Its Purposes and Functions, Op.Cit. p.58

in a purely advisory capacity. This council meets in Washington, D.C., at least four times a year with the Board of Governors conferring on the general conditions of the Federal Reserve System.(11)

The Federal Advisory Council, as provided in the Federal Reserve Act, was to have the following powers: "(1) To confer withthe Board of Governors on general business conditions throughout the country. (2) To make representations concerning matters within the jurisdiction of Board of Governors. (3) To obtain information and make recommendations for banking and credit policy in their own districts and for the system as a whole."(12)

The structure of the Federal Reserve System when placed in the actual financial set up of the country, makes a very complicated organization. Its influences are felt beyond the confines of membership in the Federal

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(11) Board of Governors of Federal Reserve System, Op.Cit. p.58

(12) Bradford, F.A., Op.Cit. p.337

Reserve System.

The "money market" is the point where banking and business interests are brought together.[13] The modern means of communication have joined the country into one large money market. When funds are needed in one city or section of the country, the money market stands ready to serve the needs of business, by being replenished from other sections where it is more abundant. Banks are the most important though not exclusive, agency supplying the funds.[14] It is through the flow of these funds that the banks all over the country keep in contact with the money market, and thus any action on their part has an influence on the market.

It is the duty of the Federal Reserve authorities to watch over the market and to set the various rates of interest and discount rates. These influences are felt by the banks,who in turn pass it on to the money market.[15]

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(13) Board of Governors of the Federal Reserve System, Its Purposes and Functions, Op.Cit. p.59

(14) Ibid, p.59.

(15) Ibid, p.61

Federal Reserve policies also affect the banks toward prospective borrowers. When funds are abundant, banks lend more freely than when they are restricted to the Federal Reserve policy. These influences on the money market are felt by both member and non-member banks, due to the abundance of money as set up by the Federal Reserve policy.(16)

(16) Ibid. p.61.

Conclusion

Unlike the British Credit System which grew up in almost complete freedom from legislation, the American banking system required government regulation, out of which developed the Federal Reserve System.(1) In constructing this new system, it was impossible to use existing banking habits as the basis for legislation, but it was necessary to take those banking practices that had been useful in other countries and adopt them to fit the already existing conditions of our country. In doing this job of remodeling, it was necessary to make the constructive changes without a slow up in the every day banking operations.

The Federal Reserve Act will and has proved to be one of the most constructive contributions ever made by Congress.(2) It is not in its final state, but as new problems and situations arise, substantial changes will have to be made in order to keep abreast with new demands.

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(1) Warburg, Paul M. The Federal Reserve System, _Its Origin and Growth_, Vol. 2. The Macmillan Company, N.Y. p.441.

(2) _Ibid_, p.442.

It will be the bankers of the United States upon whom the future of American banking will fall. They must plan and organize, not with an eye on tomorrow but for a larger future and for the benefit of all. (3)

Prior to the Federal Reserve Act there was no central organization to protect the banks or any methods of converting assets into cash. With the development of the Federal Reserve System, the country was divided into twelve central districts with a Reserve Bank in each district. (4) The two main functions provided for by these central banks was first, to provide a means of meeting the country's Gold requirements, and second, to provide the machinery for turning member bank's assets into credit or cash.

In recent years the most important problem confronting the Federal Reserve System has been in connection with the war. A great amount of planning was necessary in order

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(3) Ibid, p.442-443

(4) Ibid, p.447

to finance the war effort.(5) It was necessary to maintain a stable market in which both the Government and industry could receive credit promptly and at low costs. This was accomplished by the Federal Reserve System by purchasing Government obligations at par, by low money rates, by arranging credits for war production and by restraining the use of credit for speculation in securities. This left the country in possession of money far greater than it needed in peacetime and almost in a state of inflation.(6)

The Federal Reserve System when established was in an era of scarcity and limitation on expansion. Arising out of the war, it is now operating in an era of abundance and expansion.(7)

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(5) Board of Governors of Federal Reserve System, The Federal Reserve System, Its Purposes and Functions, The National Publishing Company, Washington, D.C., -p.114.

(6) Ibid, p.115.

(7) Ibid, p.115.