

C. Clearing House Certificate



Description

This section is from the book "[Business Law - Case Method](#)", by William Kixmiller, William H. Spencer. See also: [Business Law: Text and Cases](#).

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Story Case

In the panic of 1907, when practically every clearing house association in the United States sought to relieve the currency stringency by the issue of clearing house certificates, the association of Morton City followed the common plan. Engraved certificates, in denominations of \$5, \$10, and \$25, were signed by the officers of the association and issued to member banks in exchange for [deposits](#) with the clearing house of high grade bonds, securities, or commercial paper. The certificates recited that they were secured in that manner, and stated that they would be received by any member of the clearing house in [payment](#), at face value, of any debt or obligation, and that they would be accepted by the clearing house from any member bank which presented them in payment of balances due. One of these certificates was received by Victor Griffith in the course of business. He took it to the clearing house and presented it for payment. He was told that no one, not a member of the clearing house, would be given any credit for a certificate, and that the clearing house had not assumed to pay the certificates to any holder. He brought suit against the clearing house committee, on the ground that whatever their intention, they had, in fact, issued obligations of the clearing house. Is he entitled to recover?

Ruling Court Case. Philler Vs. Patterson, Volume 168 Pennsylvania State Reports, Page 468; Volume 47 American State Reports, Page 896

Thirty-eight [national banks](#) in the city of Philadelphia, formed a clearing house association, for the settlement of balances. A room was hired and fitted up at the expense of the associated banks, and a manager employed who presided over the business of striking the balances every morning at a fixed hour. To facilitate the settlement of daily balances without the necessity of handling and counting the cash in every case, each bank deposited in the hands of certain persons, called the Clearing House Committee, a sum of money, or its equivalent in good securities, to be used in paying the daily

balances. For these sums the committee issued certificates which were used in lieu of the cash they represented. The committee was also authorized to receive from any member of the association, additional deposits of bills receivable and other securities, and issue certificates therefor in such amount, and to such percentage thereof as may in their judgment be advisable. They agreed to accept the additional certificates if issued in payment of daily balances at the clearing house, on the [condition](#) that the securities deposited therefor, should be held by the committee in trust for the payment and redemption of the certificates.

Patterson, the defendant herein, signed a promissory note for \$5,000, for the accommodation of the Spring Garden National Bank, which was a member of the clearing house. . The bank deposited this with the clearing house committee, as security for certificates issued to the bank. When the Garden National Bank was not able to meet its obligation to the clearing house, Philler, as manager thereof, brought suit upon this note, as part of the bank's security, against Patterson, the maker of the note.

It was contended by Patterson that national banks had no authority, by law, to enter into such an arrangement as herein outlined, and, accordingly, the certificates issued were void, and the certificate being void, the security could not be enforced against him.

Mr. Justice Williams said: "We are unable, therefore, to see in what respect these banks have violated the statutes of the United States, relating to national banks, or have transcended the limits which these statutes have drawn about the business of [banking](#). They have diverted none of their funds, embarked in no new undertaking, entered into no business alliance, but devised and adopted what seems to be an improved method for doing a portion of their own necessary work. This same method, or one identical in general outline, has been adopted by the banks in every great city in the United States, and by many in other lands, and, as far as I am aware, it has nowhere been held that the method is illegal. On the contrary, it has recommended itself by its economy of time and labor to the several banks, and, by its incidental results in promoting mutual helpfulness and confidence, has come to be regarded with favor by the general public." Judgment was given for Philler.

Ruling Law. Story Case Answer

The clearing house certificates in ordinary use are not designed for circulation nor for negotiation. They are merely convenient forms of [receipts](#) or credit memoranda. An early development of clearing houses was the adoption of a clearing house fund, so that, instead of carrying each day the debit balances to the clearing house in money and the credit balances back to the bank vaults, the balance would be merely added to or subtracted from the balance with the clearing house. Each member bank deposits a certain amount of money with the clearing house, so that it may be a debtor bank for several clearings without being required to bring out any more actual cash. Besides having an account balance, upon which it may draw or against which a balance could be charged, it was found convenient to issue certificates to the banks when they deposited gold or securities. These certificates could be held by the bank until it was necessary to [increase](#) its credit with the clearing house, when they would be turned in, or they might be to some extent transferred from one member bank to another. The small denomination certificates, issued in emergencies for circulation, are not at all identical in function with the usual certificates. It was found that the associated banks could safely "pool" their security holdings, and upon them could issue these instruments, convenient for circulation, which because of the combination of strength would have the confidence of the public and be accepted in common payments. But the certificates are not promises to pay money, and there is no liability upon them as such. They will be received in payment of amounts due and are valuable only because the constant necessity for making such payments gives them a channel in which they displace money. In the Story Case, Griffith is not entitled to sue on the certificate, and judgment should be given for the defendant.