

Operation of the National and Federal Reserve Banking Systems

HEARINGS BEFORE THE COMMITTEE ON BANKING AND CURRENCY UNITED STATES SENATE

SEVENTY-SECOND CONGRESS

FIRST SESSION

ON

S. 4115

A BILL TO PROVIDE FOR THE SAFER AND MORE
EFFECTIVE USE OF THE ASSETS OF FEDERAL RESERVE
BANKS AND OF NATIONAL BANKING ASSOCIATIONS, TO
REGULATE INTERBANK CONTROL, TO PREVENT THE
UNDUE DIVERSION OF FUNDS INTO SPECULATIVE
OPERATIONS, AND FOR OTHER PURPOSES

PART 2

MARCH 28 TO 30, 1932

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CONTENTS

Statement of—	Page
Ayres, Leonard P., vice president Cleveland Trust Co., Cleveland Ohio	251
Ball, Edward, representing Du Pont-Ball Co. and Atlantic National Bank, Jacksonville, Fla.....	293
Bruce, Howard, chairman of the board of the Baltimore Trust Co.....	456
Burgess, W. Randolph, deputy governor of the Federal reserve bank in New York City.....	497
Burke, James Francis, general counsel the Pittsburgh Clearing House Association, Pittsburgh, Pa., and a former member of the Committee on Banking and Currency of the House of Representatives.....	441
Hanes, R. M., representing the Wachovia Bank & Trust Co., Winston-Salem, N. C.....	489
Hecht, R. S., president Hibernia Bank & Trust Co., New Orleans, and chairman economic policy commission of the American Bankers' Association.....	225
Houston, P. D., chairman board of the American National Bank, Nashville, Tenn.....	534
Kent, Fred I., director of the Bankers Trust Co., Scarsdale, N. Y.....	508
McQuaid, W. R., president of the Barnett National Bank, Jacksonville, Fla.....	278
Marsh, Spencer S., vice president and cashier National Newark & Essex Banking Co., Newark, N. J.....	209
Meyer, Eugene, governor Federal Reserve Board, Washington, D. C.....	357
Ottley, John K., president First National Bank, Atlanta, Ga.....	315
Payne, William K., chairman of the board Auburn-Cayuga National Bank & Trust Co., Auburn, N. Y.....	329
Platt, Edmund S., New York City, vice president Marine Midland Corporation of Buffalo, N. Y.....	310
Pole, J. W., Comptroller of the Currency, Treasury Department, Washington, D. C.....	422
Preston, Thomas R., Chattanooga, Tenn., president the Hamilton National Bank.....	323
Rand, George F., president Marine Trust Co., Buffalo, N. Y.....	479
Wakefield, L. E., president First National Bank, Minneapolis, Minn.....	339
Wolfe, O. Howard, cashier the Philadelphia National Bank, Philadelphia, Pa.; president the Association of Reserve City Bankers; vice president Pennsylvania Bankers' Association; member economic policy committee of the American Bankers' Association; and manager Philadelphia Loan Agency of the Reconstruction Finance Corporation.....	263
Zimmerman, Charles F., president First National Bank of Huntingdon, Pa., and president State Bankers' Association of Pennsylvania.....	304

OPERATION OF THE NATIONAL AND FEDERAL RESERVE BANKING SYSTEMS

MONDAY, MARCH 28, 1932

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met, pursuant to adjournment on Friday, March 25, 1932, in Room 303, Senate Office Building, at 10.30 o'clock a. m., Senator Smith W. Brookhart presiding.

Present: Senators Brookhart (presiding), Walcott, Fletcher, Glass, Wagner, Bulkley, Barkley, and Costigan.

Senator BROOKHART (presiding). The committee will come to order. We will hear Mr. Rudolph Hecht as the first witness.

STATEMENT OF R. S. HECHT, PRESIDENT HIBERNIA BANK & TRUST CO., NEW ORLEANS, CHAIRMAN ECONOMIC POLICY COM- MISSION OF THE AMERICAN BANKERS' ASSOCIATION

Senator BROOKHART (presiding). You may proceed whenever you are ready, Mr. Hecht.

Mr. HECHT. Mr. Chairman and gentlemen of the committee, on behalf of the economic policy commission of the American Bankers' Association, I, as its chairman, ask for the privilege of filing with your committee a brief official statement, and I shall then be glad to give such further testimony as you may care to have me give in my individual capacity as president of the Hibernia Bank & Trust Co. of New Orleans.

Senator GLASS. Might I ask right here, has your American Bankers' Association met and passed on this as its official statement?

Mr. HECHT. The commission has conferred on it, partly in person and by wire, with those who were not able to be present. But the formal statement which I present expresses the views of the commission.

The functions of the economic policy commission are to "give consideration to all questions involving money and currency, public finance, and the economic policy of the Government, including the economic aspects of laws and regulations governing the several classes of banking organizations."

Accordingly, our commission has given careful study to the provisions of Senate bill 4115 and has attempted to analyze them not from the selfish viewpoint of the banking interests, but from the broader and more important viewpoint of the public interest and the economic welfare of the country as a whole.

We will, therefore, confine our comments to the more general aspects of the proposed legislation leaving it to others to point out more in detail the objections to the bill from the standpoint of the practical operations of the banks.

Banking, being a semipublic business, must necessarily be controlled by strict laws governing its operations. Nevertheless, banking in its actual operations can not be conducted by statute, nor is it feasible to substitute rigid rules enforced by public officials for individual initiative and responsibility.

The human element must always remain a major part of banking operations and any attempt to take important practical operating details out of the hands of individuals and have them function automatically under rigid statutory formulas would be unworkable and dangerous.

You can no more take the human element out of banking by legislation than you can put morality into people by mere statutory enactments. Of course, banking like all other lines of human endeavor has made many mistakes and has done things which—in the light of recent events—have proven unwise and perhaps indefensible. However, it seems safe to say that the bankers of this generation have learned important lessons from these events and are determined that banking shall benefit from them. No doubt some new legislative enactments are desirable and bankers more than anyone else want to cooperate to prevent a repetition of the disastrous experiences of the past two and a half years. It seems not likely, however, that the mere transfer of the responsibility from one set of human beings, that is, the officers of banks, to another set of human beings, that is the officials in Washington, will prove a panacea for our financial ills or be a guarantee against a repetition of the same errors of human judgment in the future.

Admittedly the Federal reserve authorities should have broad powers of supervision over the general financial policies of banks and to some extent over their practical operations. But it is extremely doubtful that the enactment of such a law as now proposed which largely centralize control over detailed operating functions of banks in the hands of Government officials in Washington would improve the situation.

After all it must be remembered that not a few of our business leaders and bankers have heretofore expressed the view that much of the blame for the undue speculation and consequent later collapse of 1929 attaches to the "easy money" policy of the Federal Reserve Board then in office. It matters not whether we agree with that criticism it is mentioned solely to emphasize the fact that officials in Washington are no less subject to errors of judgment than are bankers in New York or elsewhere, and consequently a further increase of the power of Government officials over the banking structure is not necessarily a guarantee for better banking.

But granted that some changes are desirable in our existing laws the present would hardly seem a propitious time for enacting new and far-reaching provisions which in their very nature are highly deflationary. The Federal reserve act which is admittedly a masterpiece of financial legislation was evolved only after several years' study and careful deliberation, and on the whole it has proved sound and well adapted to the needs of the country.

It would be most unfortunate if we were now to rush in and attempt to cure the evils of the past few years by means which even if they proved helpful at some future time would inevitably add to the length and depth of the present depression.

For over two years we have been struggling with the most difficult and complicated business situation in our history.

Many important and necessary adjustments have had to be made, and we are just emerging from an atmosphere of hysteria and fear, which was the unavoidable consequence of this period.

More recently the passage of two relief measures, the Reconstruction Finance Corporation act and the Glass-Steagall bill, made possible by the broadminded nonpartisanship leadership of both parties, has done much to reestablish national confidence on the part of bankers and the public.

The passage of this bill would undoubtedly destroy the most if not all of the good that has been accomplished along this line, and would lead to further deflation of securities and restriction of credit at a time when just the opposite influences are needed.

The fact that three years ago an unduly large amount of credit was extended to stock-market operators by member banks, nonmember banks, as well as corporations and individuals, over whom bankers had no control, should not now cause us to go to the other extreme and attempt to enact a law which would make all the legitimate investment business an outlaw business by practically preventing banks from extending credit to those engaged in that line. Nor to the fact that in the past a few banks went too deeply into the security markets, by now using that as an argument in favor of prohibiting all banks from dealing in sound investment bonds.

Let us take care that in trying to devise means to prevent a repetition of the old mistakes we do not commit new and greater errors by destroying the machinery for the distribution of long-term securities, which, after all, are an essential part of the Nation's financial business and therefore an important public service.

In aiming to penalize speculative credits in view of past instances we should not make all banks suffer by making them pay a higher rate on their 15-day notes even when secured by United States Government obligations.

Such a provision would in turn force the United States Treasury to pay a correspondingly higher rate on its financing, with the result that interest on all classes of bonds would go up and the market price of existing securities would continue to go down.

During the period of war depression when the membership of the Federal reserve system was largely limited to national banks, a special committee was appointed to induce banks operating under State charters to join the system. They were loath to do so because they did not wish to surrender their charter rights and make themselves entirely subservient to the authority of the Comptroller of the Currency and the Federal Reserve Board. But after many conferences a satisfactory understanding was reached which assured member banks operating under State charters such reasonable autonomy and freedom of action as they felt was necessary.

As a result a large number of State-chartered institutions joined the system, which they did largely as a patriotic measure, and to-day

approximately 40 per cent of the reserve of the Federal reserve system is contributed by such voluntary members.

It stands to reason, however, that this situation will quickly change if the Federal authority over all member banks is increased a good deal and the normal operations of member banks are made subject to further burdensome official dictation by the Federal Government.

In fact, the definite statement has been made to our commission by some of the largest and best managed banks operating under State charters that the passage of this bill in its present form will lead to their prompt retirement from the system; and we think there is a danger that even national banks may deem it advisable to accomplish the same result by surrendering their national charters.

Such a development would be deplorable because the Federal reserve system has been a tower of strength since its very inception, and nothing should now be done to wreck it by making either the compulsory membership of national banks or the voluntary membership of State-chartered institutions unduly burdensome and unattractive through too much bureaucratic control in Washington.

On the subject of branch banking our association has gone officially on record, at its Cleveland convention in 1930, as favoring a limited extension.

There exists some difference of opinion in our commission as to the advisability of extending the privilege to cover an entire State. However, we held unanimously to the view that the granting of permission to national banks to establish branches in adjoining States, not over 50 miles distant, would constitute a species of trade area branch banking which would give national banks an unfair advantage over their State bank competitors whose State governments could not authorize them to establish branches beyond their own jurisdiction.

We have previously expressed the belief that some control of group and chain banking will ultimately become necessary, but we are not in sympathy with the extremely drastic provisions now proposed by depriving groups from voting on directors of Federal reserve banks, nor the retirement as to reserve and double liability, which are practically impossible to carry out.

Some supervision over the activities of affiliates of member banks is no doubt desirable, but many of the proposed provisions appear to us entirely too drastic and as unnecessary for the purpose of exercising reasonable control over their affairs.

The provision for segregating some of the best assets of a bank for the benefit of one class of depositors; that is, time depositors, would undoubtedly cause uneasiness on the part of demand depositors who would not be so secured. This would be particularly felt by country banks where a large proportion of the deposits are time deposits and where heavy withdrawals of demand deposits might result.

We do not believe that past experience justifies the radical increase proposed in the reserve requirement on time deposits. If enacted into law the burden would fall heaviest on member banks located in cities where there is no Federal reserve bank. The provision would either force a reduction in interest paid on time deposits or an increase in rates on loans.

Moreover, it would in no small measure increase the gold reserve to be carried by Federal reserve banks and would largely counteract the benefits of the Glass-Steagall bill.

The various sections of the bill referring to real-estate loans appear to us to be combersome, discriminatory, and unsound. Moreover, we consider them impractical of operation.

We have on several previous occasions made similar recommendations as to the minimum requirements of capital for new banks, and find ourselves in thorough sympathy with the proposals now made.

We are also in sympathy with the objects expressed in the bill to provide some means for the prompt liquidation of assets of closed banks. We feel that the burden proposed to be put upon member banks to accomplish this purpose is too heavy, but we should like to see Senator Glass introduce a separate bill designed to carry into effect his general thoughts on that subject, so that it might receive prompt and unbiased consideration on its own merits, free from the controversial questions connected with the present bill.

In conclusion we desire to repeat our introductory statement to the effect that we consider the passage of this bill in its present form would be untimely and inadvisable. We believe that it would destroy much good that has recently been accomplished by the remedial measures that have been adopted calculated to stop deflation; that it would weaken rather than strengthen the present banking situation.

This is not meant to say, of course, that the subject of new banking legislation should not be given due consideration. We believe that some changes in our banking laws that have been enacted are shown by experience to be desirable. But we believe that just what those changes should be can be determined only by careful deliberation, and we pledge our own services and we are confident bankers as a whole will be glad to cooperate in working out a desirable solution to the problems presented.

Senator BROOKHART (presiding). Any question by any members of the committee?

Senator FLETCHER. Of what bank are you an officer?

Mr. HECHT. President of the Hibernia Bank & Trust Co. of New Orleans.

Senator FLETCHER. Is that a member bank?

Mr. HECHT. Yes, sir. It was one of the earliest State banks to join the Federal reserve system. We joined it in the very beginning.

Senator FLETCHER. Have your demand deposits decreased or increased within the last 12 months?

Mr. HECHT. They have been almost stationary. There has been perhaps a slight decrease, but not more than 1 or 2 per cent at most.

Senator FLETCHER. How has it been with regard to your time deposits?

Mr. HECHT. It was the matter of time deposits, wasn't it, that you are speaking about? Or did you refer to demand deposits?

Senator FLETCHER. My first question referred to demand deposits.

Mr. HECHT. Oh, well. Our demand deposits have decreased during the past 12 months something over 12 per cent.

Senator FLETCHER. How about time deposits?

Mr. HECHT. Time deposits have changed very little. Oh, it might be 1 per cent difference.

Senator GLASS. Time deposits generally have greatly increased, have they not?

Mr. HECHT. In the last 12 months?

Senator GLASS. Within the last four years.

Mr. HECHT. Oh, yes; within 4 years they have increased, but not within the last 12 months.

Senator GORE. What was it that you said happened in the last three or four years?

Mr. HECHT. I think time deposits as a whole have increased in the last four years.

Senator GLASS. Say during the last six years, since we reduced the reserve to 3 per cent, they have very greatly increased, have they not?

Mr. HECHT. I would not have associated the fact—

Senator GLASS (interposing). I am not assuming what you may associate it with. But what about the fact?

Mr. HECHT. It would be very difficult for me to fix the time limit or six years, or even four years. But time deposits for the last number of years, excepting the last two years, have undoubtedly shown a tendency to increase.

Senator GLASS. They have not only shown a tendency to increase but have, in fact, very largely increased, have they not?

Mr. HECHT. I do not think they have increased very much out of proportion to other deposits. Deposits of all banks have shown a large increase over a number of years, but I have not before me statistics that would enable me to very definitely answer your question.

Senator FLETCHER. That does not apply to the last 12 months?

Mr. HECHT. Not to the last two and a half years.

Senator FLETCHER. Have postal savings banks interfered with your deposits?

Mr. HECHT. I should not think they have interfered with deposits in cities so much, but they have taken a great many deposits in the smaller banks in the country, in neighborhoods where bank failures have occurred. Whenever uneasiness develops over the failure of one bank in a given country district there is the natural tendency of persons to put their money into the Postal Savings System.

Senator FLETCHER. Have you had many failures in New Orleans during the last year?

Mr. HECHT. In New Orleans we have had no bank failure in 25 years.

Senator FLETCHER. That is a pretty good record.

Mr. HECHT. But in Louisiana we have had a very few bank failures. But at that we have not had more than 10, I should say, in a year.

Senator FLETCHER. Have your loans increased or decreased in the last 12 months?

Mr. HECHT. Well, they have not increased, and yet they have not decreased as much as we would like to have them decrease.

Senator FLETCHER. You mean that you are devoting your attention to collecting sums due your bank rather than making new loans?

Mr. HECHT. Of course, a bank could hardly have a shrinkage of 12 per cent in its deposits and not make some efforts to collect in

some of its loans, because it could not meet its obligations if it did not do so.

Senator FLETCHER. What kind of securities do you outline in the matter of your loans?

Mr. HECHT. Well, of course, in New Orleans, we being at a port where it is quite natural that commodities would play a very important part in our activities, cotton, sugar, rice, all commodities that pass through the port of New Orleans form a very considerable percentage of our collaterally secured loans. But we are, of course, in other respects the same as other banks in cities, we loan to commercial institutions and we loan on good collateral of all kinds.

Senator FLETCHER. Do you loan much on real estate?

Mr. HECHT. Well, we do so more indirectly than directly. We loan to country banks large sums of money, who in turn, of course, are lending largely on the basis of real estate. We do not make a large percentage of direct real-estate mortgage loans.

Senator FLETCHER. Do you not approve of one feature of this bill that would tend to a separation of real banking from the merchandising of securities?

Mr. HECHT. I should say that the tendency to limit the activities is perfectly correct, but the unscrambling of affiliate corporations, which over a period of the last 15 years have been closely tied up with banking institutions, appears to me to be very difficult and in some respects a dangerous procedure.

Senator GLASS. Do you think they should ever have become tied up with commercial banking institutions?

Mr. HECHT. Senator Glass, may I answer your question in this way? If the bill presently under discussion were a bill that we might all consider for the purpose of starting the ideal banking system upon a fresh basis, then there would be a good many provisions in it which I would strongly favor. But under existing conditions, and because of the difficulty and the harm that would come from their enforcement I am now opposed to them. In other words, it is one thing to have a theoretical opinion whether banks should ever have gone into the investment business in the past, and it is another question whether we should now, by one swoop of the law, try to undo something that has grown up over 20 years of banking practice.

Senator FLETCHER. But if it is bad practice the sooner you quit it the better.

Mr. HECHT. I am not prepared to say it is bad practice. I am prepared only to admit that there has been cause for criticism in the operation of some security affiliates. I am not prepared to say it is not a perfectly natural function for banks to deal in high-class investment securities, either through bond departments or through security affiliates. It is only an abuse of the thing that is bad; it is not the thing itself that is bad as I see it.

Senator FLETCHER. Have you any affiliate?

Mr. HECHT. Yes; we have. We have the Hibernia Securities Co., which is an affiliate converted from the bond department of the bank as it had been previously operated. That was done some 14 or 15 years ago.

Senator GLASS. Then, I assume your theory is, if an evil practice of long standing has associated itself with the banking business, it ought never to be corrected.

Mr. HECHT. No. I would not make any such statement or demand. And I have not admitted that it is an evil practice. I have stated that it is the abuse of the practice that has justified criticism now being leveled at it, and that it requires perhaps some additional legislative control.

Senator GLASS. Oh, now, I understood you to say at the outset that you did not believe in statutory restrictions at all, that the matter ought to be left to the judgment and management of the banks.

Mr. HECHT. I beg your pardon, Senator Glass. You could hardly put on my language any such meaning as that, because I started out to say that banks necessarily must be governed by strict laws in their general operations, but that that does not mean all the detailed transactions passing through a bank can or ought to be governed by law and leave nothing to the private initiative and judgment of the banker who is running the bank.

Senator GLASS. I understood, well down in your thesis, that you said you were opposed to statutory regulations, or to supervision that we might some of us say was severe, or that I would say was of a vigilant character, by the board supervising control.

Mr. HECHT. I made the statement that a bank being a semi-public business must necessarily be controlled by strict laws governing its operations.

Senator GLASS. Yes; but what else did you say?

Mr. HECHT. But there is a limit most assuredly. That is exactly my position. You can not govern every banking transaction by a law that is going to be controlled in Washington.

Senator GLASS. Do you think this bill undertakes to govern every banking transaction in Washington?

Mr. HECHT. No; but it attempts to govern a good many more than are feasible, in my opinion.

Senator GLASS. Do you think it confers any more important authority upon the Federal Reserve Board, for example, or upon Federal reserve banks, than they already possess?

Mr. HECHT. Yes; I certainly do, in many respects.

Senator BARKLEY. When would you be willing to begin correcting such evils as you admit exist in the present banking system?

Mr. HECHT. There are perhaps some that might be well corrected rather promptly, but such important questions as the control of real estate loans, control of loans on collateral security, and measures of that kind, that are undoubtedly deflationary, will add to our present troubles, which in my judgment should not be discussed or at least enacted at this time, but should await a return, not to another boom period but at least to a more normal period in banking, when general confidence is not already shaken as badly as it is now.

Senator GLASS. You do not think we ought to correct things that have shaken public confidence.

Mr. HECHT. I do not think we should do anything that will lengthen the present depression, that will continue or add to the fear and hysteria on the part of the general public that already exists.

Senator GLASS. Doesn't the existing law undertake to control the volume of real estate loans made by institutions engaged in commercial banking?

Mr. HECHT. Not to anything like the extent that this bill now proposes. Why, you would have to liquidate more real-estate loans under this bill than you could possibly hope to liquidate in normal times even in a good many years.

Senator GLASS. But, of course, we do not think you would have to liquidate any more such loans.

Senator BULKLEY. Mr. Hecht, I should like to hear upon what basis you make that statement.

Mr. HECHT. Well, for instance, there is the question of real estate owned by banks, and real estate owned by affiliates of banks, and the calculation of what loans you could make on real estate when you take into consideration, as this bill appears to do, the ownership of the banks' own buildings. It would just utterly make it impossible within a 2-year period to comply with the provisions of this bill without the sale of an enormous amount of real estate.

Senator FLETCHER. Do you object to the limitation as to amount of loans on real estate being based on percentage of deposits?

Mr. HECHT. Well, I am objecting to it under its present form. I am not prepared to say there should not be some limitation, and as a matter of fact there are some limits now.

Senator BULKLEY. What do you think would be the amount of liquidation that would be required?

Mr. HECHT. That is a pretty difficult question for any man to attempt to answer and give a horseback opinion.

Senator BULKLEY. Then you are prepared to say it would be disastrous without having the slightest idea of what it would be in fact?

Mr. HECHT. No, but I would have to study the situation. I can illustrate it by giving a few concrete examples of institutions I do know something about, of banks that happen to have some buildings of their own, and have a certain amount of real-estate mortgage business, that could not under any circumstances comply with the provisions of this bill without forcing the sale of an enormous amount of real estate, or else increasing the capital stock of their banks by such an absurd amount as to make it just as impossible.

Senator BULKLEY. But I should like to get any specific information you may be able to give us as to that fact.

Mr. HECHT. I do not know that I would care to mention the names of any particular institutions, but I can repeat the statements I have already made, that—

Senator BULKLEY (interposing). Here is my trouble: I do not want to criticize your intent in the matter, but a good many people come in here and make criticisms in so vague a way that we can not put our finger on them, and they come to conclusions that we do not agree to, and then leave the matter so far up in the air that there is nothing for us to go upon. I should like to have any other information you may be able to give us in order that we may either say you are right, or else understand that you can not give us an intelligent answer.

Mr. HECHT. Well, Senator, the difficulty is that to be specific in figures on what you are now asking me a man would have to be prepared to get together some data and give you specific facts.

Senator BULKLEY. But how can you possibly reach the conclusion that you state without any knowledge of the figures?

Mr. HECHT. I do not admit that I do not have any knowledge.

Senator BULKLEY. What knowledge have you? Let us get it on the record.

Mr. HECHT. I have already made the statement that I could name, without giving the name of the institutions, any number of banks.

Senator GORE. Can you give a hypothetical case that would parallel one of those actual cases?

Mr. HECHT. Why, yes; very easily.

Senator GORE. Give us that.

Mr. HECHT. You take a bank that may have \$5,000,000 of capital and surplus and it has a bank building that may be on its books for three and a half or four million dollars. There are any number of such cases as that. It might also have a certain amount of mortgage business besides. But the bank of that magnitude would have a good many real estate loans. Under this provision not only would the Comptroller revalue the real estate which they are carrying, which to me appears to be an impossible task in times such as we are living in now, because I do not know what the market value of any real estate is just now, but in addition to that the real estate owned by that bank, plus the mortgage business that they may normally do, plus the real estate that they may have money loaned on more or less against their will that they may have taken as collateral security after a loan was made, would certainly so far exceed the limitations in this bill that that bank could not under any condition within two years put itself in shape to comply with the provisions of the bill.

Now, how many times that case can be multiplied I am not prepared to say, but I should say that there are hundreds of cases, to be conservative, that would be in that class of cases.

Senator BULKLEY. Is that an actual case, Mr. Hecht, that you have just given?

Mr. HECHT. Yes.

Senator BULKLEY. You have given us actual facts?

Mr. HECHT. Yes. There are several cases where the figures are almost identical where this description would fit.

Senator BULKLEY. What is your opinion as a banker of the condition of that bank as a commercial banking institution?

Mr. HECHT. Senator, the question comes right back to what I said a moment ago. If they were starting from scratch and were trying to lay down laws of what is good business for a bank to do in the way of encouraging it to own its own bank building or office building, I might be inclined to say that the bank was unwise in going that far. But at the same time, there were circumstances that make that a perfectly sound transaction. In the several cases I have in mind I know the return is perfectly satisfactory, and while it may not be what you and I would do if we started to-day, still to undo that all over this country would do a great deal of harm.

Senator BULKLEY. Now let us avoid the hypothetical question of what we might do if we were starting all over again. I would like to know your opinion about whether that is a good sound condition to-day or whether it is a bad condition.

Mr. HECHT. It is not necessarily an unsound or bad condition at all.

Senator BULKLEY. You think that is all right for a commercial bank to be in the position that you have just stated?

Mr. HECHT. I think that the four or five banks that I have in mind in what I am speaking about are perfectly sound, good banks.

Senator BULKLEY. I do not mean to question that, but I am asking you whether you think that is a good condition for a commercial bank to be in.

Mr. HECHT. I think it is a perfectly safe condition for the particular institutions to be in. I am not prepared to say that there may not be some other banks where it is not a good condition.

Senator BULKLEY. We will have to measure the value of your conclusions in the light of that opinion expressed, that that is a sound and proper condition for a bank to be in.

Mr. HECHT. Well, Senator, you have no right to put more in my statement than I have put in it.

Senator BULKLEY. I do not mean to put a bit more in it. I want to get your own statement.

Mr. HECHT. I think it is not possible to lay down a hard and fast rule and say that a thing is sound or unsound, because circumstances alter cases, and there are many good banks that are in that position that are just as safe and safer than banks that have no bank buildings at all; but I have no doubt that there are other banks that have gotten themselves into a tight position as a result of such unwise investments.

Senator BARKLEY. Let us suppose that your hypothetical bank that has \$5,000,000 of capital and surplus has three and a half or four million of it invested in a bank building, and let us suppose that the value of that bank building has gone down to \$2,000,000. You are still valuing it on the books at three and a half or four—I don't mean you, but your bank. Supposing that the Comptroller of the Currency should take the same position with reference to that that he has taken with reference to the deflation of the value of bonds. What would be the result of that? Many banks have been closed because of the deflation of the value of bonds in which the capital and surplus of the banks have been invested—that is true, is it not?

Mr. HECHT. Yes.

Senator BARKLEY. Suppose the Comptroller of the Currency took the same position with reference to the enormous decrease in the value of real estate. What would be the result?

Mr. HECHT. Senator, there could only be one result.

Senator BARKLEY. Yes.

Mr. HECHT. And that would be disaster.

Senator BARKLEY. What is the difference, though, in the soundness of the security?

Mr. HECHT. Senator, I do not believe the man lives who could go over these United States to-day and tell you or me what the value, the market value, on all the bank buildings is in the United States to-day. I do not think anybody can do that.

Senator BARKLEY. No; but we all know that there has been a considerable deflation in real-estate values.

Mr. HECHT. That is true, and yet the rentals from these bank buildings probably have not changed at all; but I admit if you tried

to sell these buildings to-day you would unquestionably have to take a very severe loss.

Senator GLASS. Do you believe in the existing law and in the requirements as to the judgment of the comptroller in writing off bad loans?

Mr. HECHT. Why, yes; of course.

Senator GLASS. Do you think if he were to do that now he would not close about 60 per cent of the existing banks?

Mr. HECHT. I should hate to think that there was any such percentage as that, Senator, but no doubt that would close some banks.

Senator GLASS. I have heard it put much higher than that by experienced bankers.

Mr. HECHT. Well, of course, I would leave it to the comptroller to make that estimate. I would not care to hazard a guess of that kind. But I would not like to add to his difficulties.

Senator GLASS. You do not think the law ought to be enforced, then, do you?

Mr. HECHT. No; I do not say that. I think the comptroller is quite capable of reaching his own conclusions on that. I think he is doing the right thing in the valuation of high-class bonds. I think that has been a very sound practice on the part of the comptroller in not attempting, just because there are a few chalk marks that say a bond that is perfectly good and gives a good return and is high class in every respect, that a bank should write down its surplus because 5 or 10 bonds have sold at a certain price. I think the comptroller on the whole has pursued a very sane and sensible policy.

Senator GLASS. I am not questioning that, but it is not a policy in conformity with the practice in ordinary times, is it, under the law?

Mr. HECHT. Well, he has undoubtedly made some modifications. The one I have just spoken of is the best example. I do not happen to be a national banker, and I am not perhaps in as close touch with that as I might be.

Senator GLASS. What more reason is there requiring a comptroller to require banks to write off depreciated stocks and bonds that does not apply to real estate?

Mr. HECHT. For the simple reason that I do not think it is possible to determine the value of real estate with anything like the accuracy that you can determine the value of securities. I just do not believe any real-estate appraiser in the land is capable of that.

Senator GLASS. Do you think the value of securities were very accurately determined in 1928 and 1929?

Mr. HECHT. They were very accurately determined from the standpoint of their salability. Too many of us made the mistake in not selling them, but they were certainly salable at that time.

Senator BROOKHART (presiding). Wasn't that the time when this hysteria that you talk so much about occurred?

Mr. HECHT. It was another type of hysteria, Senator; yes. There was just as much hysteria in 1929 on the bull side of it as there is hysteria at the present time in fear and lack of confidence.

Senator BROOKHART. This thing you call hysteria now simply is cautiousness against the hysteria we had in 1928 and 1929?

Mr. HECHT. No, Senator; I would go a little further than that I would say that, taking the value of securities in 1929, the question of earnings or anything of that sort did not enter into it apparently. Things were boomed up to an unreasonable point.

Senator BROOKHART. That was all hysteria, was it not?

Mr. HECHT. That was hysteria; yes.

Senator BROOKHART. And the bankers had just as much in that as anybody else?

Mr. HECHT. I am not excusing the bankers from making out any better than the average man. But I say that now the same is true; that earnings and general values have just as little to do with quoted prices on the exchanges as they had in 1929, because they have gone down just as much below their intrinsic value as they were above their intrinsic value in 1929.

Senator BROOKHART. I have here an Alexander Hamilton Institute chart which shows the value of those bonds, 95 stocks, are still, to-day, as high or perhaps slightly higher than they were in the war-inflation period of 1919.

Mr. HECHT. Well, of course, I am not familiar with the chart that you have or know anything about it, but the question of what stocks are picked out there and all that would enter into it. I would not care to discuss that without knowing what I was referring to.

Senator BROOKHART. There is another chart of the Federal Reserve Board, with all 337 of them, showing about the same condition of the whole output of stocks.

Mr. HECHT. What do you call the inflationary period of the war?

Senator BROOKHART. 1919 is what I am referring to here. That is the high period until 1921.

Mr. HECHT. Of course, I am not an expert on stocks, and I do not pretend to have any opinions on them; but just thinking in my own terms of the large corporations in this country, and thinking of their values to-day as compared with 12 or 14 years ago, I am sure that they are selling far below their 1919 quotations to-day.

Senator BROOKHART. The Alexander Hamilton Institute would be quite reliable?

Mr. HECHT. I should think it ought to be; but I repeat, I prefer to stick to banking and not express opinions on stock exchange operations, because I know very little about that.

Senator BROOKHART. Well, but you have come here before us and want to maintain these affiliates with the banks that deal in stocks and bonds.

Mr. HECHT. I am to begin with not thinking of affiliates in the terms of dealing in stocks.

Senator BROOKHART. You limit them to bonds altogether?

Mr. HECHT. Yes; I think the investment business is not a stock business.

Senator BROOKHART. Bonds themselves are behind the stocks, though, are they not?

Mr. HECHT. They come ahead of them, not behind them.

Senator BROOKHART. Well, ahead of them. They are part of the same organization?

Mr. HECHT. But in quality they do vary materially from stocks.

Senator BROOKHART. But a bond may be watered just as easily as a stock?

Mr. HECHT. Most assuredly, yes; but it has security behind it.

Senator BROOKHART. Were you in the National Credit Corporation that was organized by the banks?

Mr. HECHT. Yes, sir.

Senator BROOKHART. To help themselves and to take care of this situation?

Mr. HECHT. We were.

Senator BROOKHART. And that did not get very far?

Mr. HECHT. We loaned out in our particular section in Louisiana and Mississippi some eight or nine million dollars.

Senator BROOKHART. And how much was altogether? You have quit now, haven't you?

Mr. HECHT. About one hundred eighty million, if I am not mistaken.

Senator BROOKHART. Out of the five hundred million that was subscribed?

Mr. HECHT. Yes, sir; approximately that. Some of it has been paid back.

Senator GLASS. You subscribed how much?

Mr. HECHT. We subscribed to 10 per cent of our capital and surplus.

Senator BROOKHART. How much did you ever pay in?

Mr. HECHT. We paid in 30 per cent of that. In our case, with five hundred fifty thousand subscription, we paid in 30 per cent, one hundred sixty-five thousand, of which 15 per cent is being paid back to-day, the first payment.

Senator GLASS. Do you regard that as a very great burden?

Mr. HECHT. Not under the circumstances.

Senator GLASS. Why, then, do you regard this one-half of 1 per cent, or really one-quarter of 1 per cent assessment, of this liquidating corporation burdensome?

Mr. HECHT. I think there is a little difference there, because what we were doing in subscribing to that, we were helping out our own immediate situation in Louisiana and Mississippi, which was of course very close to our hearts. In this we would be a little further removed from it, but I have indicated that so far as the provision of the liquidating corporation was concerned, while I think that is a little too high, I have no serious difference of opinion with you on that whole plan.

Senator GLASS. What percentage would you assess the banks?

Mr. HECHT. My objection to it, frankly, Senator, was more on the proportion of the Federal reserve contribution who would have to put in very little cash, and the banks who would have to put up a proportionately large amount. Of course, you may say that was offset, but my opinions on that are so nearly the same as yours that I do not believe that if we had that bill under consideration by itself it would be very difficult for me to agree with you, except that I still might want to argue a little about the proportions, but I do not think I would even want to oppose the bill itself on that ground.

Senator GLASS. The proportion would be just as burdensome in a separate bill as in this, would it not?

Mr. HECHT. Yes, it would be. I have only made the statement that I thought the proportions might be adjusted to some extent, but

I repeat, I have no such fixed opinion that I would not be glad to support the bill if it had to be on that ground.

But I would like to just come back and answer your question perhaps a little more specifically why I was more willing to put my money into the National Credit Corporation so freely and not in here, because one was a strictly temporary measure and we were all assured it would be temporary, and the other would be a rather permanent thing.

Senator GLASS. You had some other assurance, didn't you, that the Government was going to take it over?

Mr. HECHT. Well, we heard about the plans for the Reconstruction Finance Corporation.

Senator GLASS. But Mr. Pope stated to us here the other day that you were very definitely assured.

Mr. HECHT. I was not in Washington, so I am not prepared to make the statement one way or the other.

Senator BROOKHART. You did understand there was some such assurance?

Mr. HECHT. We had understood that the Reconstruction Finance bill was under consideration and that its operations were to cover this particular feature.

Senator BROOKHART. You supported the Reconstruction Finance Corporation?

Mr. HECHT. Yes, sir.

Senator BROOKHART. You wanted the Government to step in and take charge of things in that regard then?

Mr. HECHT. We were entirely in sympathy with the proposal that was made.

Senator BROOKHART. Yes, but now you are opposed to the Government taking any further steps to stop another inflation such as we had in 1928 and 1929?

Mr. HECHT. No, I am not opposed to that at all. I am only asking the Government not to try to do something that will get us deeper into the depression than we are to-day, and that is exactly what is going to happen if this bill passes in its present form.

Senator BROOKHART. Supposing the Government would prohibit banks from using their credit at all in speculation in any way. That would be more drastic than this bill provides?

Mr. HECHT. If such a thing were possible that would be very fine, but I do not know just how you are going to tell everybody—

Senator BROOKHART (interposing). You do not think it is possible?

Mr. HECHT. No, sir.

Senator BROOKHART. Are you familiar with any of the cooperative banking systems of the world?

Mr. HECHT. In a broad way.

Senator BROOKHART. Do you know about the English?

Mr. HECHT. In a general way only.

Senator BROOKHART. The German systems, Raiffeissen and Schulze Delitzsch?

Mr. HECHT. I know something about it; yes.

Senator BROOKHART. You know that the constitution of the organization prohibits the use of credit for speculative purposes?

Mr. HECHT. I am not prepared to say, though, that I would want the American banking system to come down to that, because you might cure 1 evil and create 10 new ones. That is about what would happen.

Senator BROOKHART. Yes; but you know that any of those systems is sounder and has not had the failures and shakeups of things and values or anything else that our system has in our country, do you not?

Mr. HECHT. Yes. On the other hand, they have not had either the development or the prosperity that this country has had.

Senator BROOKHART. They were also hit a hundred times harder by the war and more than we were?

Mr. HECHT. Yes; that is undoubtedly true.

Senator BROOKHART. There is really no occasion for the great shake-up and the number of failures in our Nation except bad management and very largely in the banking system?

Mr. HECHT. Overexpansion, and I am not attempting to defend the bankers in their share of it, but, Senator, the public at large takes matters into their own hands. When they want to speculate, when a man comes into my bank and he has United States Government bonds and borrows money on them, I can not ask him whether he is going to loan it out on Wall Street or whether he is going to buy stocks with it or what he is going to do.

Senator GLASS. Why can't you? They do it in Canada. They do it in Great Britain.

Mr. HECHT. Do you mean to say, Senator, in Canada the people have not speculated in the markets as American business people have speculated in the markets?

Senator GLASS. Have they had any bank failures up there in this whole period?

Mr. HECHT. That has nothing to do with the—

Senator GLASS (interposing). I mean to say this: I mean to say if you were a business man in Canada and are accustomed to have a line of credit with your bank, that that bank requires you at the beginning of your fiscal year or before the beginning of your fiscal year to bring in your statement and tell what you are going to do with the money that you borrow. Is that not a fact?

Mr. HECHT. I am not prepared to say it is or not, because I never lived in Canada.

Senator GLASS. To me it is a most amazing statement for anybody to say that a bank has not any right to inquire of its borrowers what they are going to do with the money.

Mr. HECHT. I have not said that we haven't any right to ask, but I said we had no control over what the man does when he gets the money.

Senator BROOKHART. You have control over letting him have the loan?

Mr. HECHT. Perfectly true.

Senator BROOKHART. And you do inquire, do you not, all the time what he is using that money for?

Mr. HECHT. We certainly have in recent times, because we have had good reasons for wanting to know.

Senator GLASS. You found no difficulty in disclosing these facts in answering our questionnaires. Banks of the country gave a very intimate, and we assume accurate, statement of what was done with the money loaned.

Mr. HECHT. Well, if banks can give an accurate statement of what their clients do with the money they loan, speaking of it in broad general terms, they are undertaking a great deal. We know, of course, in many instances, but we can not pretend to—I would not want to sign my name to a statement that told you exactly what every customer who borrowed from my bank did with the money, because I just could not do it; I would not know.

Senator FLETCHER. Do you figure, Mr. Hecht, that the holders of the class A stock, say, in the liquidating corporation would expect any profit?

Mr. HECHT. Senator, I do not know.

Senator FLETCHER. You have not gone into that?

Mr. HECHT. I do not know.

Senator FLETCHER. Do you think there is anything in that provision that tends to protect depositors in banks?

Mr. HECHT. It would certainly tend to assist them. I do not know that it would protect them, but it would be a beneficial thing to do, because so much hardship results from closed banks that the unfortunates that are caught in it sometimes have to wait so long for ordinary liquidation that the purpose of that liquidation would be defeated.

Senator FLETCHER. You spoke about getting further time for consideration. Senator Glass introduced this bill in 1930, the first bill. Haven't the banks had time enough up to now to consider it?

Mr. HECHT. Yes; we have very definite opinions on it too, and the bill has not changed much since we considered it 60 days ago, and times have not changed much.

Senator FLETCHER. Have you reached any view as to the cause of the terrific decline in price levels, commodity prices?

Mr. HECHT. Only the opinion that the pendulum swings from one extreme to the other. It went entirely too high and out of reason in 1929.

Senator FLETCHER. You mean it did that with reference to excesses in speculation and so forth producing the financial crisis, but this depression reaches another stage, and that is the decline, unprecedented decline, in commodity prices, price level. Is that due to an absence of purchasing power?

Mr. HECHT. Well, of course; speculation, Senator, is not limited to securities. Speculation was just as strong in commodities at different times as it has been on securities. But there is no doubt that the purchasing power of people generally has been greatly reduced and that the lower prices are the effect of that reduced purchasing power to some extent.

Senator FLETCHER. Have you any theory about how to help that situation?

Mr. HECHT. No; I do not believe there is any panacea for the curing of that ill except a gradual, normal, steady return to prosperity, and a reestablishment of confidence that will allow people to go

about their business in a normal way and not be dominated by fear and hysteria, as they have been dominated during the past year.

Senator BROOKHART. Don't you think it is quite as important that they be no longer dominated by the hysteria of speculation?

Mr. HECHT. Yes; I do.

Senator BROOKHART. Isn't that the thing we need to stop?

Mr. HECHT. Yes; I do.

Senator BROOKHART. You mentioned that other countries did not have the growth and development of the United States. What has been the development of the United States since 1928?

Mr. HECHT. The same as all the rest of the world. It has just had the same depression that has existed—or at least in 1929, of course.

Senator BROOKHART. We had a national wealth value in 1928, according to the National Industrial Conference Board estimate, of 360 billions. But it dropped to 329 billions in the same estimate in 1930, and then in 1931 it has gone very much lower than that. So that means that we have not had growth and development in the United States, does it not?

Mr. HECHT. Quite certainly; but, if you compared the same figures that you are now giving me for the United States, with which I am not familiar, with those of other countries, I imagine perhaps the percentage of decline in this country was, to say the least, no greater than anywhere else.

Senator BROOKHART. Well, I am familiar with one other. I know the Soviet Government has advanced a good deal more than we have declined.

Mr. HECHT. That is probably correct. You have me at a disadvantage when you compare these figures, Senator. I am not familiar with them.

Senator GLASS. Mr. Hecht, in the course of your argument you very severely decry the power of bureaucracy, and generally speaking I am in sympathy with the criticism, if we really mean bureaucracy. But you had special reference to section 11 of the bill authorizing banks to borrow on their direct promissory notes for a period of 15 days. You understand that under existing law the Federal Reserve Board has unrestricted power to fix the rate of that sort of borrowing, do you not?

Mr. HECHT. Yes; I do.

Senator GLASS. You would deprive it of that right?

Mr. HECHT. No; but you are depriving it of the right of fixing a 1 per cent higher rate.

Senator GLASS. I am fixing a minimum. The Federal Reserve Board, for example, in 1928 and 1929, knowing, if it did know, that this provision of the law was being perverted to stock-speculative purposes, had the right to fix that rate without limit, had it not?

Mr. HECHT. That is my understanding.

Senator GLASS. An extraordinary power, is it not?

Mr. HECHT. It has never been exercised in any way that has been embarrassing to anyone.

Senator GLASS. No; the failure to exercise it has been embarrassing to the whole country and has brought us to this state. That is what we are talking about now.

Mr. HECHT. I do not see where you are going to cure that by arbitrarily fixing a rate of 1 per cent on the best collateral that

banks bring to the Federal reserve bank and fix a 1 per cent higher rate than you do on other collateral. I do not see how that is going to cure it.

Senator GLASS. Well, we think we know how it will cure it. It will transfer the protection of the 15-day paper loan to eligible paper required by the act instead of letting it rest wholly on bonds.

Mr. HECHT. Well, Senator, you mean—

Senator GLASS (interposing). Let me ask you this: When this provision was put in the act two and a half years after the system was in operation and for a specific purpose, I assume, being a well-informed banker, you know what the purpose was. Suppose we had never had a World War and the Government of the United States had retired its bonded indebtedness, which, at the time this provision was put in, was less than a billion dollars, what would have happened with that provision?

Mr. HECHT. Senator, I do not think I would care to express any opinion as to what would have happened if business conditions had been as different as they probably would have been if we had not had a World War.

Senator GLASS. You could not have borrowed under that provision under United States bonds, could you?

Mr. HECHT. We probably would not have needed to. Probably we would not have the scarcity of commercial paper that we have to-day. Probably we would have had a period of mortgaging, where people borrowed on commercial paper to finance themselves on preferred stock and otherwise, and so reduced the amount of eligible paper that banks in many sections find extremely difficult to have enough strictly eligible paper to keep themselves in comfortable position.

Senator GLASS. How many banks and in what sections?

Mr. HECHT. Why, a great many banks and in many sections, outside perhaps of the financial centers of New York, Chicago, and Philadelphia and a few other cities. I am not prepared to name them all. But I should say that the scarcity of eligible paper is very general, and the percentage of eligible paper held by member banks is to-day smaller than I believe it has ever been, or certainly it has been in many, many years.

Senator GLASS. The chief of the bank operations of the Federal Reserve Board supplied me with the official figures showing that the banks had an aggregate of \$3,069,000,000 of eligible paper at that last report and \$5,500,000,000 of United States bonds; that only 91 banks out of the 7,000 in the system were without eligible paper, and that at the time the banks had \$8,500,000,000 of usable paper they were discounting to the extent of less than a half billion dollars.

Mr. HECHT. Well, of course, when you put all of those figures together they may sound as if there was a large supply of eligible paper, but when you—

Senator GLASS (interposing). Well, there was \$3,000,000,000 of it.

Mr. HECHT. All right, but it does not do a bank in New Orleans or Birmingham or Nashville or in the West or anywhere else any good to have a lot of eligible paper in the portfolios of the banks of New York and Chicago, when in their own particular communities the eligible paper is very limited.

Senator BULKLEY. How many banks in the whole Atlanta district are short of eligible paper?

Mr. HECHT. I am not prepared to answer that question without having statistics before me, but I should say that their percentage of eligible paper in the Atlanta district, I should say I would be very glad and it would be very interesting for me to do it, to furnish you with that information, and I think it will bear out the statement that I make that it is smaller to-day than it has been for many years.

Senator BULKLEY. I think maybe Senator Glass can furnish it to you and that you will be surprised.

Mr. HECHT. I would be very interested. I happen to be a director in the New Orleans branch.

Senator GLASS. Would you be surprised that in the operations of the Federal reserve system reported to me it shows that there were two banks in the Atlanta district that had no eligible paper?

Mr. HECHT. Well, Senator, I am not speaking of banks that have no eligible paper; I am speaking of the banks that have not a percentage of eligible paper that we in the past felt a well-run bank should have. I am not talking about the banks that were in distress.

Senator GLASS. But you were not using the paper that you had.

Mr. HECHT. You can not make that statement, Senator, without having the facts before you.

Senator GLASS. I do not make it without having the facts before me. I am giving you the facts that were furnished me officially.

Mr. HECHT. Yes; but that still does not tell you that there may not be a great many banks that are short in their percentage of eligible paper, and I repeat my statement, and I will furnish it officially, that the percentage of eligible paper held in the Federal reserve district that I know anything about is smaller to-day than it ever has been or certainly has been in many years.

Senator GLASS. And yet it was so great that \$3,000,000,000 of it were on hand unused?

Mr. HECHT. No; I am speaking of the Federal reserve district that I know something about. You are taking figures there taking in New York banks and Chicago banks and Philadelphia banks that are in an entirely different class from the average city banks scattered over the country.

Senator GLASS. The report showed the distribution of eligible paper over the whole country.

Senator BULKLEY. I think Mr. Hecht will furnish for the record that data of which he speaks as soon as he can.

Mr. HECHT. I want to say that I will do that, because I want to really support my statement so far as my own Federal reserve district is concerned. I am not prepared to discuss it on the others.

Senator GLASS. Well, going back to section 11 of the bill relating to stock speculative operations and the use made of Federal reserve facilities to promote stock speculative operations: You do not think that the Federal Reserve Board should have any means of enforcing its orders in matters of that sort?

Mr. HECHT. I mean that raising the interest rate 1 per cent is not going to have the slightest effect on it.

Senator GLASS. That is just one-half of one sentence of the provision. I am asking you now if you think the Federal Reserve Board ought to have authority to enforce that requirement. Eliminating the 1 per cent altogether, it now has unrestricted right to fix any rate it pleases. Suppose it should fix a rate of 1 per cent, 2 per cent, 5 per cent. Do you think it ought to have any authority to enforce its rate?

Mr. HECHT. Enforce its rate?

Senator GLASS. Yes.

Mr. HECHT. Yes; I think so; most assuredly.

Senator GLASS. What authority would you give them to enforce it?

Mr. HECHT. Well, they have the authority now.

Senator GLASS. I know they have, but they have no means of enforcing it. Don't you recall that when the Federal Reserve Board undertook what they called "direct action" the board was flouted and told to mind its own business and that a certain bank in New York was going to do as it pleased about this?

Mr. HECHT. Yes; but that did not prevent the Federal Reserve Board from raising its rate if it wanted to.

Senator GLASS. No; it was attempting to operate by direct action. You do not think then that we should authorize the Federal Reserve Board to suspend a bank for a certain period as in its judgment it should in order to enforce its decree?

Mr. HECHT. That is a pretty broad question, Senator, that I think the subject is so much abused that I hesitate to say that it should have that privilege. I think the Federal Reserve Board and the banks have a good deal of control over their member banks in many other ways without suspending them from the system. I believe that if it ever came to that a bank would certainly resign from the system before it would permit itself to be suspended.

Senator GLASS. Do you think they exercised that control in 1928 and 1929?

Mr. HECHT. No; I do not think they did, but that is just what I am contending, that the Federal Reserve Board is made up of so many human beings, subject to just so many errors of judgment, the same that bankers and business men everywhere else are subject to errors of judgment, and it is always so easy two and three and four years later to point out mistakes of others, when perhaps if we had been in their place we might not have done any better.

Senator GLASS. Congress is made up of so many human beings whose judgments are subject to error and mistake. Upon that theory, then, you would not permit Congress to embody anything in a statute of a restrictive nature, would you?

Mr. HECHT. Quite the contrary. I have always believed in our democratic form of government, and whenever the majority decides what should be done, that satisfies me, but I also assert—

Senator GLASS (interposing). Here in this provision we do more than that: We require more than a majority. We require six out of seven members of the Federal Reserve Board to enforce a penalty. Is it not reasonable to suppose that if the six out of seven members of the Federal Reserve Board should say to a bank in New York or elsewhere, "You are too greatly extended in your speculative loans and we will not make you any further loans until you re-

duce or decline to extend your speculative loans," that would be in accordance with your theory?

Mr. HECHT. I should say if the directors in the Federal Reserve bank in any given district made their report to that effect to the Federal Reserve Board in Washington, and some one tried to defy both the directors of the Federal reserve bank and the Federal Reserve Board, there would undoubtedly be mighty good cause for some action.

Senator GLASS. That is what this thing provides. After due warning by a Federal reserve bank or board.

Mr. HECHT. I am not speaking against that provision particularly. It does not appeal to me as being a desirable one, but at the same time I have no serious argument against that, so long as it comes up through the Federal reserve bank in the district that would know the circumstances better than they could be known at a distance.

Senator GLASS. That is what the bill requires. It requires a warning from the Federal reserve bank or board.

Mr. HECHT. Personally, I can not conceive—

Senator GLASS (interposing). Then I understand your objection to that provision is confined to the minimum of 1 per cent increased rate?

Mr. HECHT. Well, and its general limitation on collateral loans. I am not now just clear what is in section 11, but I am not laying any stress, in any event, upon the point that you make.

Senator GLASS. It does not make a general limitation upon collateral loans. It simply says to a bank that if it is far extended in its collateral loans—

Mr. HECHT. Yes.

Senator GLASS. And is duly warned to desist by a Federal reserve bank or board, it shall desist.

Mr. HECHT. Of course, you have that paragraph in your mind so clear and I have not, that it is a little hard for me to categorically reply.

I repeat that a provision of that sort is not at all to my personal liking. I can not conceive, speaking more personally as a director, that I could ever get myself in a position where such a thing could happen to me, but I have no particular argument against that unless that power were abused, which I do not think it would be. I do not see that any great harm could come from it.

Senator GLASS. You said that you believed in democracy.

Mr. HECHT. Yes.

Senator GLASS. And the majority rule. This requires the concurrence of six of the seven members of the board.

Mr. HECHT. I repeat I can not conceive any bank putting itself in such a position, but if it so defied that authority as a member bank I suppose some such drastic action might well be justified.

Senator BULKLEY. And you do agree with this then, the 1 per cent penalty rate is a limitation of credit control rather than an extension of it?

Mr. HECHT. No; I do not.

Senator BULKLEY. You do not?

Mr. HECHT. No; I do not.

Senator BULKLEY. I thought you agreed a few minutes ago that the board had a right to fix any rate.

Mr. HECHT. Yes; but what I just say now, force them to do that.

Senator BULKLEY. That is what I am saying; I am saying that you agree with me that their power is restricted and not enlarged.

Mr. HECHT. Yes; their power is restricted, but on an unfavorable basis.

Senator BULKLEY. But that is another question.

Mr. HECHT. Yes.

Senator BULKLEY. I just wanted to get the question of bureaucratic control settled.

Senator BARKLEY. I want to ask this question, which is probably a question broader than the scope of this bill, but this man seems to be a very intelligent banker, if not above the average intelligence even for bankers.

Mr. HECHT. I do not know if that is a slam or a compliment, Senator.

Senator BARKLEY. It is intended as a compliment. I am very much concerned—of course we all are—about a permanent solution of this banking question, not looking with any degree of pride more than anybody else, perhaps, to the fact that last year twenty-three hundred and some odd American banks failed; whereas in no other country in the world, or in all of them combined, were there that many failures. So that there is something fundamentally wrong with our banking system. While the larger number of bank failures in that year can be attributed to the depression, in normal times when we delude ourselves into the belief that we are prosperous, there are entirely too many bank failures.

Have you thought out a remedy for that situation that is permanent? Would you be willing to suggest, if you have, what we can do to prevent that situation from existing in this country?

Mr. HECHT. Senator, I am not going to be conceited enough to believe that I have any remedy for that very deep-seated problem, but I do not mind expressing at least some general views on the subject. I think the bank-failure record is a most unfortunate one for the last two years, but it has been due to abnormal conditions. So, let us in answering your question come back to what you yourself have pointed out, that even in normal times we have a good many bank failures.

I would only say this: That I think that if you analyze the bank failure record in normal times you will find that, while the number has grown, it is usually among very small units; and my opinion is that the tendency is going to have to be by an evolution of a process of the concentration into, not great, big units of having a dozen banks in this country like they have in Canada, which I am very much opposed to, but at least the concentration of these extremely small units, which can not under existing economic conditions be on a profitable basis; and a bank that is not profitable is sooner or later going to fail. Therefore, if we can gradually eliminate the very small unit by combinations, mergers, or other means, I think we shall go a long way toward at least improving materially the bank failure record of this country. Proper supervision over State and national institutions, of course, must also play a very important part in that.

Senator BARKLEY. Do you think our dual system of banking has anything to do with that?

Mr. HECHT. No, I do not. I am afraid I am, perhaps, a little prejudiced on that subject, Senator, being a State banker; but I do believe that there is a place in the banking structure of this country for the dual banking system if the dual banking system is not used to make unfair competition. I have fought many times, and I am prepared to fight now, against any discrimination that would make it difficult for a national bank to compete properly with a State bank. I am in favor personally, and not speaking for my commission, of the extension of branch banking on a state-wide basis. Where the State banks are permitted to do it, I think it would be an unfair disadvantage for a national bank not to have that same privilege. In other words, I believe that there should be an equality of opportunity for the two systems on a sound basis. I do not think there should be competition to see how much more loosely one bank will be permitted to do business than another, but I still believe that the dual banking system has its proper place in our scheme of things in this country.

Senator BARKLEY. That is a profound subject and too long to try to enter into here.

Senator BROOKHART. I do not want to close that without one suggestion about these small unit banks. Is it not true in our country for 55 years they got along quite as well as any units?

Mr. HECHT. Yes, that is true, Senator; and I do not want you to misunderstand me. What I am referring to is that the bank in the county seat has its place and will always have its place, but the improvement of roads and the concentration of business into some one community have made it well-nigh impossible for a lot of the country banks that had not a \$15,000 capital to get along.

Senator BROOKHART. The big banks in the country went into speculative business and drew the little banks into it themselves. The little banks do not have any particular trouble.

Mr. HECHT. Of course, I can not share your opinion on that because I think the trouble with little banks has been from the unfortunate condition of agriculture. I think that anything we can do to improve the agricultural situation will cure the evil of the country bank that has the problem in being able to earn enough money.

Senator FLETCHER. Do you think there ought to be a requirement of more capital, both for the State banks and the national banks?

Mr. HECHT. Yes. I think very small banks are not going to be able to operate profitably, and I think the limits for the establishment of new banks, both State and National, should by all means be raised.

Senator BROOKHART. I shall have to close this now.

Senator WAGNER. I just want to ask one question. Mr. Hecht, you stated previously that in your own State you had an unusual record in the number of banks closed. In the city of New Orleans, I understood you to say, there were none that failed.

Mr. HECHT. None over 20 years.

Senator WAGNER. In the whole State during this period of depression there were how many?

Mr. HECHT. What would you call the period of depression? Twelve months, or shall we go back further?

Senator WAGNER. Two years.

Mr. HECHT. In two years I should estimate there were probably not over 30. Maybe less, but I think 30 would be an outside figure.

Senator WAGNER. How does that compare with other States?

Mr. HECHT. Very favorably.

Senator WAGNER. Do you attribute that to the fact that you have not been hit as severely by the depression in your State?

Mr. HECHT. No.

Senator WAGNER. Or is it better supervision?

Mr. HECHT. I think our agricultural situation has been fully as bad as it has been anywhere else with cotton and sugar and rice having been at such low levels, but I think our bank supervision on the whole has been very satisfactory and our record of failures in our State over a long period of years has compared very favorably with other States.

Senator BROOKHART. You have had small unit banks at all times?

Mr. HECHT. We have a great many; yes. Senator, in our State you can have county branch banking, and that is what has happened down there in a good many instances where the very small bank went in with the bank in the county seat.

Senator GLASS. You know a large part of our trouble in legislation, Mr. Hecht, has been caused by the dual system of banking. Whenever we tried to do something to make the national banking system sounder than it is and to put it upon a high plane, we have always been confronted by the objection that that puts a national bank at a disadvantage with the State bank.

Mr. HECHT. That may be true, Senator. On the other hand the 48 States of the Union have their right and privilege to govern their own banking system, and I do not see how they are going to get away from that.

Senator GLASS. I am pointing out the difficulties that we have in applying sound legislation.

Mr. HECHT. I realize that, and I have made the statement that the thing I have always stood for was that the competition between the two systems should be in respect to how good they can be made and not how loose the methods can be under which they operate.

Senator GORE. Louisiana had an exceptionally good banking system at the time of the Civil War.

Mr. HECHT. Yes. It dates back.

Senator GORE. Prior to the banking act system. What are your total deposits?

Mr. HECHT. In my own bank about forty to fifty million dollars.

Senator GORE. What is the percentage of time deposits?

Mr. HECHT. About 25 per cent of that, or a little more.

Senator GORE. What interest do you pay?

Mr. HECHT. A maximum of 3 per cent.

Senator GORE. What per cent do you pay on your demand deposits?

Mr. HECHT. None at all on a good portion of it, and a maximum of $1\frac{1}{2}$ per cent.

Senator GORE. What per cent of your demand deposits do you pay?

Mr. HECHT. I should say probably one-third; maybe a little bit more than that.

Senator GORE. Could you estimate what percentage of your demand deposits result from the deposit of cash or cash items and what proportion from the loan discount operations?

Mr. HECHT. I think that is a very difficult question to answer. I do not believe I could give you that per centage right off, Senator. It would be a pure guess.

Senator GORE. You stated a minute ago in response to Senator Barkley's question that a large part of the failures in this country compared with other countries was due to the depression.

Mr. HECHT. Not compared with other countries, because I do not think we can compare our system in the number of failures with that of any other country, for the reason there is not other country that has anything like the banking system we have.

Senator GORE. That is true, but we have had the depression.

Mr. HECHT. But you know what has happened in the other countries except England and France. In France there have been a good many substantial failures, but the banking was concentrated. The Government and banking are closely affiliated. In Germany you know the Government has actually subscribed preferred stock in two of the large banks in order to save them from failing. They would have failed.

Senator GORE. What I was trying to get at is this: That that is a condition that is universally applicable to all countries, so we have got to seek the weakness in our system of banking and find that to account for the failures here.

Mr. HECHT. I am not prepared to admit that in percentage of total resources the failures in this country would compare unfavorably with what the failures might have been in Germany, for instance, if the Government had not stepped in, or in Norway and Sweden, where they had their banking troubles and the Government stepped in.

Senator GLASS. Our Government stepped in here to the extent of \$2,000,000,000 in one bill.

Mr. HECHT. \$200,000,000 so far, Senator.

Senator GLASS. I say, the Government has stepped in to the extent of \$2,000,000,000, has it not?

Mr. HECHT. Well, it has not advanced the money yet. It is prepared to.

Senator GLASS. It is prepared to advance the money.

Mr. HECHT. That is what has stopped failures.

Senator GORE. Neither did the other National Credit Corporation advance the money.

Mr. HECHT. That is why we have had almost no failures in March and very few in February as compared with what we had in December and November and the months before.

Senator GLASS. That is not altogether the reason. One reason is that so many banks have already failed that there are not many more left. [Laughter.]

Mr. HECHT. If it had not been for the National Credit Corporation and the Reconstruction Finance Corporation, the number would have been just as great or greater in these three months.

Senator GLASS. That is a mere matter of opinion. I do not agree with that statement.

Mr. HECHT. As chairman of the reconstruction committee in my territory, and having also had a great deal to do with the National Credit Corporation, I am prepared to say that it is a little more than just a horseback opinion that I am giving you.

Senator GORE. This National Credit Corporation, organized by the bankers, did not advance very much money, did it?

Mr. HECHT. \$180,000,000 in all.

Senator GORE. Has not a great deal of that been advanced after it became practically certain that this reconstruction bill would pass?

Mr. HECHT. No. I think only a small percentage of it.

Senator GORE. I had in mind a big bank out on the Pacific Coast.

Mr. HECHT. Of course, I should not, perhaps, talk in percentages, because I do not know. I mean as to the time element.

Senator BROOKHART. Thank you, Mr. Hecht.

Call Col. Leonard P. Ayres.

STATEMENT OF LEONARD P. AYRES, VICE PRESIDENT OF THE CLEVELAND TRUST CO., CLEVELAND, OHIO

Senator BROOKHART. You may proceed with your statement.

Mr. AYRES. Senator, I am vice president of the Cleveland Trust Co. in Cleveland, Ohio, and also a member of the Economic Policies Commission of the American Bankers' Association.

My interest in this bill is general rather than relating to my own institution. It happens that my own institution is not directly affected by many of the provisions. It is a bank and trust company of some \$250,000,000 deposits, doing a large savings business, having, perhaps, some 440,000 depositors. It has no bond department. It has no underwritings or originations. It has no active securities affiliate, and never has had. It has no interest in any group or chain, but it has some 57 branches at the present time. So it is that my own interests in this bill become general rather than specifically applied to that institution.

Senator GORE. Are you a member of the Federal Reserve system?

Mr. AYRES. Yes, sir. It seems to me, gentlemen, that the most important thing that any of us have to think about and to deal with in America to-day is this appalling depression in which we are, in common with the other nations. We have in my own organization a somewhat active statistical division which has done a good deal of research work, and, among other things, it has in the past two years succeeded in carrying back as accurately as may be an account of the variations in business activity and industrial production in this country ever since the beginnings of the Government. It has carried it back month by month to 1790, with less accuracy, clearly, in the earlier years, but with great pains, and as accurate as the data make possible. The records show, I think, beyond any question that this is the most serious depression that the country has ever faced; that even the long and great depressions of the forties and the seventies, about which we have such dreadful stories, were less than this. Moreover, this depression is still getting worse. I think it is true that, for example, the tons of railroad freight that

the railroads of this country will originate this year will be not over half, per capita of the population, of what they were in 1913, the year before the war, and that it will be less than in any year since the depression of the nineties. It has a stoppage and cessation of business activity completely unparalleled in our history. Probably business to-day is at something like from 40 to 50 per cent below what might reasonably be termed as normal. Under those conditions it seems to me that all of us must think of public questions and proposed actions in terms of their relationships to the prospects and possibilities of business recovery; and so I have been trying to think about this bill in those terms rather than in purely technical terms.

Frankly, as I go through the numerous provisions and attempt to analyze them, it seems to me that one can hardly pick out more than a single provision embraced in two sections of the bill for which it could fairly be claimed that it probably would be, if enacted into law, an affirmatively positive help in business recovery. The one that I refer to is that provision in, I think, sections 21 and 22 that would make possible the extension of branch banking for national banks, thereby, perhaps, making it possible for some communities to have stronger banks than they now have; and perhaps one might say fairly that that would operate in positive fashion to facilitate business recovery.

As for all the rest of the bill I should believe that the provisions either would have no positive effect on business recovery, however desirable they might be in other ways for general banking conditions, or would have an adverse effect; and it seems to me that for most of them the effect would inevitably be adverse in this particular respect of thinking about business recovery. Without going into any technical consideration of them, one would for example, say that the matter of increased reserves for time deposits, provided by section 13, I believe, would require from the banks the locking up of cash resources in Federal reserve banks in amounts that may be estimated at something approximating \$130,000,000 a year for five years. Whatever that might do in the long run for the protection of time deposits, clearly its immediate effect on business recovery would not be helpful but in so far as it took that money out of current credit uses would be detrimental rather than beneficial.

Senator BULKLEY. When you say "current" of course you recall this is not effective at all until 1933.

Mr. AYRES. Yes, Senator; but we are still going to be in a depression in 1933.

Senator BULKLEY. I thought that might have some bearing on your use of the word "current."

Mr. AYRES. I think it would, and I think my use of the word "current" was misleading in that case. I was thinking of "current" as of that time rather than as of now.

Senator BARKLEY. You think it is going to be a long current? The current of this depression will last some time, to make a play on the word?

Mr. AYRES. Senator, the sad fact is that no one can study the long diagram that I referred to, that shows the fluctuations of business activity over the past 140 years and more, without realizing that in

depressions recovery has always been more slow than decline. Business always has gone down faster than it has come back. If that be true this time, it would mean that we are not yet half way through this depression, because the depression is still continuing and business is still declining. It has been doing so now for substantially two and one-half years—not quite. Should recovery start now—and I think there are a few symptoms of it—still we should be more optimistic than anything in our past history would justify if we thought we should get back to what the statistician and economist term normal business, which is a poor, unsatisfactory kind of business anyhow, in another two and a half years; so that I think we can be quite sadly confident that we have at least a long period ahead of us before we shall see that measure of recovery.

Senator BROOKHART. On that proposition, Colonel, I have here a chart that I think was prepared by you, showing half a century of American business. It ends with 1930. This chart shows 8 major depressions in the last 50 years. There were about seven little ones thrown in for good measure.

Mr. AYRES. Yes. There are eight in here if you count the nineties as two.

Senator BROOKHART. And then the line of normal business along through the middle there. I looked over that to find out how much of the time we had been normal, and I could not find 30 minutes in the whole 50 years. [Laughter.]

Mr. AYRES. No; I suppose one could not if you are thinking about a business that fluctuates in long, irregular waves from depression through recovery to prosperity, to decline, and back to depression. Of course, the moments when it is passing the equator, so to speak, are not even in the aggregate numerous.

Senator BROOKHART. Is that a sound system of business? Is not there something fundamentally wrong with the business that is going up into inflation and then down into depression all the time?

Mr. AYRES. Yes. There is something fundamentally wrong.

Senator BROOKHART. Is not part of it due to the credit system of banking?

Mr. AYRES. I believe it is myself. There is a great diversity of opinion.

Senator BROOKHART. I agree with you that we are not through this depression. That is the way it looks to me all the time. But what are the things necessary now to bring us out of this depression? What could we do that would end the depression?

Mr. AYRES. Right here the main thing we could do would be to refrain from trying to change a very complicated credit and business and banking situation and machinery, to disrupt it, to break it apart.

Senator FLETCHER. You mean, then, that we should do nothing?

Mr. AYRES. In so far as this proposed legislation goes, I personally should say that there is no feature of it that would be greatly hurt by being postponed, even the best features, and I think there are many; and that there are other features that would be harmful to enact now. I think myself that this would be the most unfortunate time in recent years to make a complete or a considerable readjustment of our business of credit extension, except, perhaps, in 1918. I think it would have been worse to remake our systems in 1918,

but with that exception I should say this is the worst time in recent years.

Senator BROOKHART. Was the Reconstruction Finance Corporation a good thing?

Mr. AYRES. I think so.

Senator BROOKHART. It was a Government bolshevik institution that we set up for the banks and the railroads mainly?

Mr. AYRES. Yes; to prevent breakdowns.

Senator BROOKHART. If it is a good thing for them, could not we do something for agriculture along the same line and restore agricultural prices?

Mr. AYRES. We have not restored prices by means of that.

Senator BROOKHART. And we are not going to, either, are we?

Mr. AYRES. I should think not, although there is some hope in it.

Senator BROOKHART. You think it would be a good thing if we did restore agricultural prices and restored the buying power of agriculture?

Mr. AYRES. Yes; and general price levels, if we could do it.

Senator BROOKHART. Could not that be done by a Treasury note issue to pay the soldiers' bonus, for instance, and to provide a billion dollar or more revolving fund for the Farm Board to handle the exportable surplus of agriculture, to take it from the domestic markets, so the price could rise?

Mr. AYRES. It could conceivably be possible by changing the value of our own dollar. However, I have never been persuaded myself that this Nation, acting alone and by itself, could lift the world levels of commodity prices. I think there is the difficulty.

Senator BROOKHART. You concede it has lifted the domestic level of the protected industries, has it not, above the world level?

Mr. AYRES. It can lift a single price, of course.

Senator BROOKHART. Well, it can lift a long list of single prices, and has done it by tariff protection, has it not?

Mr. AYRES. Somewhat; and yet it is astonishing how much the commodity prices of the world move up and down together in these long, irregular waves.

Senator BROOKHART. They move up and down, but the American level stays all the time above the world level.

Mr. AYRES. Not on fundamental commodities. They have world prices. Cotton has a world price.

Senator BROOKHART. But cotton goods are a different thing from cotton in that respect.

Mr. AYRES. Yes. But it is so if one take cotton and wheat and rye and copper and tobacco, and so forth.

Senator BROOKHART. All of those are things we export. There is an exportable surplus.

Mr. AYRES. Yes.

Senator BROOKHART. I am talking about the domestic things now that we produce under the protective tariffs at home. Those maintain a higher price level than the world, do they not?

Mr. AYRES. Many manufactured goods do.

Senator BROOKHART. That is what I am talking about.

Mr. AYRES. Oh, yes.

Senator BROOKHART. We have maintained that right along by this artificial process called a protective tariff system?

Mr. AYRES. In part; yes.

Senator BROOKHART. Agriculture has had to pay that kind of a price for the things it buys under that system. Is not agriculture entitled to such governmental assistance as would give it that kind of a price for its products?

Mr. AYRES. That last question is beyond the thoughts that I have been marshalling for this matter. I hardly want to say.

Senator BROOKHART. I suppose it is; but I would like to get you thinking about it and see if it would not help get out of this depression.

Mr. AYRES. I am very glad to think about it. I think that everything that relates to a possible way out ought to be thought about by everybody that can do the thinking.

Senator BROOKHART. If agricultural exports are less than 10 per cent, on an average, of the production, the 90 per cent that is consumed at home could, under our Federal power, be protected up to a cost of production level, could it not?

Mr. AYRES. That is exceedingly difficult, sir.

Senator BROOKHART. It could be done, though?

Mr. AYRES. I should not say it could not be done or that, by that and other measures, these prices might not be lifted.

Senator BROOKHART. Since we maintain this artificial price level for manufactured products in the country, is it not a foolish thing to let the world fix a price of our agricultural products when there is only on an average about 10 per cent of them that goes into the world market?

Mr. AYRES. Not over 17 per cent.

Senator BARKLEY. Is it not true that there is a much larger percentage of the agricultural products that go into surplus than 10 per cent? You take cotton.

Senator BROOKHART. No. I will give you those percentages if you want them. There is a little over 50 per cent of cotton. That is the biggest item. About 20 per cent of wheat; 7 or 8 per cent of livestock products; less than 1 per cent of corn; less than 1 per cent of oats.

Senator BARKLEY. Of course where we consume all of any product we make, the world price would not have anything to do with it except that it might regulate our imports to a certain extent; but we can not lay down a hard and fast rule with reference to products where we export and where our market and our prosperity depend upon imports.

Mr. AYRES. No.

Senator BROOKHART. But if we have only 1 per cent of corn, the biggest of all agricultural products, exported, is it right that that little 1 per cent should fix the price of the other 99 per cent here at home, when the corn farmer must buy in a protected market of a higher level than the world?

Mr. AYRES. Well, one may answer that, Senator, in either way. One, of course, might follow out his answers in the terms of attempting a complete protection, or in the other direction, in the terms of eventual equalization by reducing the barriers for the other

things, so that we would have a very long discussion of the two types of possibilities and their ramifications.

Senator BROOKHART. Our protective system is now so firmly established that it would bring disaster on the country if we should abandon it suddenly and go to world free trade, would it not?

Mr. AYRES. Oh, quite so. We can not do any of those changes in a day.

Senator BROOKHART. Regardless of whether you believe in this original thing or not.

Mr. AYRES. Yes.

Senator GLASS. Mr. Chairman, if I may venture and make a comment: It seems to me that here we are doing what we habitually do in the Senate and discussing matters that are not related to the measure we have under consideration.

Senator BROOKHART. Senator, here is the greatest statistician, I think, in the country at this time.

Senator GLASS. I know, and when you get to your cooperative proposition it would be well to summon him in and have him help you out.

Senator BROOKHART. We shall be glad to do it.

Senator GLASS. We have only two days more of this hearing.

Mr. AYRES. One might go on. I know our time is short.

Senator BROOKHART. I specifically want to get now what would bring us out of this depression that you state we are in and going deeper still, and I want to see if there are not some things that could be done that would turn that tide.

Senator GORE. If you will suggest some way to do it, we will all agree to elect you president.

Mr. AYRES. Gentlemen, I do not believe there is any short and easily applied panacea by which we may emerge from the depression. I think it is going to be a matter of teamwork along very many lines among very many kinds of people. I think we have done quite a bit already.

Senator BROOKHART. Teamwork we have not had in the past.

Mr. AYRES. I would include the Glass-Steagall bill. I would include the reconstruction bill. Now, the Reconstruction and the National Credit Corporations are things to avert breakdowns rather than constructively to build up, but they did avert some breakdowns.

Senator GLASS. Can you tell us what has been the volume of rediscounts by the Federal reserve banks under the Glass-Steagall bill?

Mr. AYRES. I can not, in figures; no, sir. But I do know this: I believe we can say that the banking crisis is by; not the difficulties but the crisis; partly because of that and partly because of reconstruction. Bank failures have stopped virtually. Credit is becoming easier. The money that was hoarded is flowing back in. We have not yet stopped the shrinkage of loans and deposits. That is still going on. And yet all over the world interest rates are coming down. There is a better sentiment in banking, and I think it is fair to say that the crisis, the banking crisis that was carrying us toward a dangerous abyss, is by, and that that is the greatest victory so far in the process that will ultimately lead us into business recovery.

Senator WAGNER. Colonel, is the shrinkage in loans due to a lack of demand for credit or is it the refusal of the banks to extend credit, in your opinion?

Mr. AYRES. I do not think it is a lack of demand. I have tried to look into that question. That is a very important question. I think there is a fair demand for enough good borrowing so that we should be greatly benefited if the banks now were more generally extending credit. We have not really switched over to a period of credit expansion, and that we ought to do.

Senator GLASS. We have heard it repeatedly stated in the public prints recently, and I imagine upon accurate information, that the banks have refused to make loans to the railroads or to renew loans to the railroads.

Mr. AYRES. Well, I suppose that the banks, seeing that that was the one kind of loan that they could, perhaps, transfer to an agency constituted for the purpose, have felt that they could better serve their commercial customers by turning over the railroad loan and making loans for constructive purposes rather than carrying the loans provided for by the Reconstruction Corporation.

Senator GLASS. The corporation was not instituted for that special purpose.

Mr. AYRES. No.

Senator GLASS. On the contrary, it predicated the power to loan to the railroads upon, not the suggestion, but the explicit requirement that they could not get loans from the banks at a reasonable rate of interest.

Mr. AYRES. Yes.

Senator GLASS. So that it was not the design of the corporation to loan a great amount of its money unnecessarily to the railroads but only if the banks refused.

Mr. AYRES. Where the corporation has done the most good. I think, is in constituting a place toward which the bank or the railroad or the other organization which qualifies may turn in time of need, and having a place to which it may turn, it usually does not have to turn. I think that that is what has stopped the bank failures—not that they have been borrowing much from the Reconstruction Corporation, but because the banker and the customer know that if pressure should come there is a place, and that has done it.

One might go on with the other matters: The real-estate loans. However, we may interpret the act, I suppose that we should agree that by bringing in the bank premises and bringing in loans, the eventual safety of which depends upon real estate, there would be involved at least some tightening of real-estate lending in any national bank already carrying loans up to the 50 per cent established limit. So, without pressing that too far, I think I should still include it with those other things that would not tend actively and now to aid in recovery from depression, but with the things which would have a tendency in the other direction.

Senator GLASS. Why was it, Colonel, that the national bank act for a period of 50 years prohibited commercial banks and national banks from making loans on real estate at all?

Mr. AYRES. Of course, that was the way we did our banking business when the system was established, and it represented at that time an advanced kind of highly protected—when I say “protected” I mean safeguarded—banking procedure. Then in time it was decided to modify it. The modification is in effect. I am not argu-

ing against a modification of that modification; I am arguing that we should do well to stop and consider whether it ought to be put into effect in 1932.

Senator GLASS. Colonel, do you think it is particularly encouraging to see the picture that apparently has been presented here? To me the most depressing thing, the most utterly discouraging thing that has happened in recent months, is to have an organized effort to make it appear that the banking business of the country has been so abused and misused that it has got into such a deplorable state that it can not tolerate any suggestion of remedy.

Mr. AYRES. I think it is always discouraging when one puts in his best time and thought for a purpose which he conceives to be constructive and in the public interest and then a lot of other fellows come in and find fault with it and criticize it. I do not share the type of attitude that you have described as being entertained by many, and I concede that you are right. I am still thinking along narrow grooves, Senator. I am thinking about this matter of this depression, and I have been thinking about the things that I think you were thinking about in the drafting and developing of this bill. I went back and tried to study over a very long period of more than a century what happened when we got into depressions and what happened when we got out. I think there is in this bill the assumption that we get into depressions because of, or at least after, times of overspeculation, and I think that the record supports that view. There is in the history of these things a vast diversity of conditions, but one condition that apparently is always present when we are going into a depression—that is, in the prosperity preceding the drop into the depression—is an overindulgence in speculation.

Now, that speculation is, however, very diverse in its forms. We all know about 1929, but if we go back only 10 years we must realize that we did not go into the depression of 1921 because of an overindulgence in general stock-market speculation. There was a bull market, but it was a puny thing compared to this last one. What we did that time was to speculate in commodities, and in those days we all talked in the banks about frozen inventories. Nobody talked about frozen loans. When we say "frozen loans" we may mean the customer's collateral loan, but in those days, 10 years ago, it was otherwise. If one goes back to the great depression of the forties, which was perhaps the worst depression previous to this one, and which lasted six years and was utterly disastrous, one finds that what preceded that was an unparalleled speculation in farm lands quite as active as anything we had in stocks this last time. In that period this country was the great wheat producer and exporter, and it became so prosperous in that type of agriculture that we came into the late thirties with the farmers swapping their wheat lands around among themselves so actively, with exchanges set up in every town for doing it, that for several years they did not plant the lands at all and we had to import wheat to feed the people because the speculation in land was so great that the farmers did not even cultivate it. We got along into the seventies, where our great depression of six years again took place, and we find that the speculation was a speculation in construction. The whole country went wild on construction. They constructed railroads. They con-

structed whole new towns, new mills, new houses, new bridges, turnpikes—everything. There was not much stock speculation in there. We came up to the depression of the nineties, and we had a new era just like that last one. We used the phrase "the new era" to describe it, and we had a great stock speculation; but before the depression of 1907 and 1908 it was rather a matter, if we can again use the term, of a speculation in mergers, represented, it is true, by securities, but without any very great public participation in it. It was the rich man's period, so called, and they merged about everything, until the thing crashed and we had the mass of undigested securities.

Senator WAGNER. Was not the automobile industry the factor in pulling us out of that depression primarily?

Mr. AYRES. We might say so. It was effective somewhat.

Senator WAGNER. I mean it helped to absorb?

Mr. AYRES. It helped us a great deal. I think we overcredit it, but it was a great help.

Senator WAGNER. It absorbed a great deal of the unemployment?

Mr. AYRES. Yes.

Senator BROOKHART. Does that all mean that these depressions have been caused each time by general speculation of some kind?

Mr. AYRES. Of some kind.

Senator BROOKHART. In 1840, when agriculture was the principal business of the country, if there occurred a general speculation in that, that would bring on a general depression.

Mr. AYRES. Yes.

Senator BROOKHART. You say the automobile industry probably pulled us out, but has not agriculture helped to pull us out of these depressions in the last 50 years?

Mr. AYRES. Several times over.

Senator BROOKHART. And that was due to the gradual advance in land values?

Mr. AYRES. In part, and in some cases—

Senator BROOKHART. Since 1920, when land turned back, agriculture has been unable to help pull us out of the depression?

Mr. AYRES. Yes.

Senator GLASS. The automobile business has pulled more people into difficulties than it has ever pulled them out.

Senator WAGNER. It pulled us out in 1921.

Senator FLETCHER. In reference to the seventies, you speak about the depression there being of construction. Was not that the time when Jay Cook went under?

Mr. AYRES. Cook nearly went under four years before that. Really the end of Cook's important period was Black Friday in 1869, connected with the gold situation.

Senator GLASS. Colonel, you have an intimate and accurate knowledge of these matters. Let me ask you this question: Do you know of any legislative reformation of the banking business in all these years that has not been suggested or prompted by financial disasters? Take the Federal reserve act for example.

Mr. AYRES. I would put it the other way around and I would say that people always want to reform the banking system in every big depression in this country and abroad, and have for a hundred years past.

Senator GLASS. Has it been reformed in any other period of time? Take the Federal reserve act for example. Was not that the product of the 1907 and 1908 disaster?

Mr. AYRES. I would say so. More than any other one thing, yes. Now, in the upturns from depressions—

Senator BARKLEY. I do not know whether you have admitted specific evils in our banking system or not. I do not think you have.

Mr. AYRES. I could, but it would take me quite a long time.

Senator BARKLEY. Assuming that there are specific evils that need specific remedies, when are we going to begin to administer those remedies? When we are sick, or wait until we get well? When we are well we become self-satisfied and we are afraid to do anything lest we get back into the same sickness again.

Mr. AYRES. I would not do it either time, Senator. I would do it on the recovery period. I do not think you can reform a banking system at the height of prosperity.

Senator GLASS. You can not even enforce existing law under the existing procedure.

Mr. AYRES. It is extremely difficult. And I think it is dangerous to do it at the bottom of a really serious depression, but when the tide has turned; and it is not so hard to know when that is and when recovery is well enough under way so that it has momentum. I think we ought to take the lessons of the periods through which we have come to legislate to improve the machinery.

Senator BARKLEY. Will not we be cautioned in such period against doing anything for fear it slackens the momentum of recovery?

Mr. AYRES. I suppose you would if you tried to reform everything at once. I think you might cut it up into small pieces.

Senator GORE. You say that the speculation assumes different forms but it always precedes a crisis and a depression—speculation in some forms. Does not that rather tend to prove that this speculation and these great depressions rather grew out of human nature, the tendency of men to buy on a rising market, as things would go up to buy more and sell at a profit until you reach a limit where somebody will not pay the price, they lose confidence, and they sell on the falling market, driving the price down?

Mr. AYRES. Senator, I would not question at all that that is one of the characteristics determining phenomena of these business cycles.

Senator GORE. Is not that where the difficulty lies; you have got to amend the law of human nature in order to stop that?

Mr. AYRES. It is one of the difficulties; but, Senator, we have got to move in that direction, because we can not stand many depressions like this one.

Senator GORE. Yes. They all have the same specific operations. In other words, they repeat.

Mr. AYRES. When the recovery period does get under way there is a certain uniformity, I think, that has a true bearing on the questions that we are discussing here. Every depression that we have had for a hundred years past has been followed by a business recovery in which advancing prices and advancing volumes for long-term securities took place before most other kinds of upturns occurred. It is almost the singular, uniform phenomenon of business recovery.

Senator GLASS. Is not that because long-term paper went lower in value than any other form of credit?

Mr. AYRES. I do not think there is any question that that has a real bearing on the situation, and in the initial part of the move it is a recovery of those prices from depths that daring people decided were absurdly low.

Senator GORE. Until they stay at a low point long enough for people to be convinced they are not going to go any lower?

Mr. AYRES. Yes; except daring people are trying it all the time. Their first guesses are wrong, and finally they get right. But after the upturn starts, then new issues come in, and there is where the money comes from that finances the new construction, that buys the new equipment, and that assembles the materials that put men to work and starts production to expand. What I am afraid of here is that if we too fully divorce the operations of the banking system which accumulates these funds from the operations of that other system which turns them into the long-term securities which finance recovery—if we do it before that recovery has started and throw on to our fabric of finance the job of an almost complete reorganization of its methods and its procedures, I am afraid that we shall find that we have done it just too early; that we have done it a time which makes it extremely difficult for that recovery mechanism which always has worked—and it is the only one we are sure about that has worked without exception to operate effectively.

Senator GLASS. Colonel, in order that you may be sure that members of the subcommittee of the Banking and Currency Committee did not proceed in a whimsical and arbitrary fashion to consider these problems and to treat them in a legislative way, if you will refer to the hearings that we had here—and the testimony was supplemented by personal interviews with experienced bankers and political economists who did not care to appear in public—you will find that we had, as we regard it, authoritative advice that would have caused us to abolish investment affiliates outright over a brief period of years, long enough, as it was conceived, to enable them to get at the business in an orderly way. Instead of doing that we have simply proposed to regulate them, as we conceive, in a rational way.

Mr. AYRES. It is a question of judgment, Senator. It seems to me like revising the fundamental system of the tactics of an army during a battle. This is almost a drawn battle and just being won, and I would rather wait until I was sure I was winning out before I revised the tactics.

Senator GLASS. We plan to wait. We give them three years, I think, to detach themselves from the commercial-banking business or, rather, to detach the commercial-banking business from its affiliates.

Mr. AYRES. I hope that is going to be enough time, but I would like to be sure before I put it in.

Senator GLASS. You realize, I am sure, because you have, I see, an intimate knowledge of such things—I will not say invariably, because I only have knowledge of particular instances—that when we enacted the Federal reserve bill we were confronted with the same kind of organized opposition, the same sort of bitter criticism, the same sort of threats, to the effect that no national bank would enter the system, and to the effect—a few days before the President ap-

proved the act—that the Federal reserve system would destroy the national-banking system. You recall those things?

Mr. AYRES. I remember something about those periods; yes.

Senator BROOKHART. Colonel, I would like to ask you a few questions about these cooperative systems of the world. Have they had the ups and downs of these other systems?

Mr. AYRES. Not in the same degree; no. There is a kind of stability built into them. You mean the cooperative banking systems?

Senator BROOKHART. Yes; of the various countries that have them.

Mr. AYRES. That has prevented that degree of fluctuation.

Senator BROOKHART. Are the two things in those that make for stability, first, they never use the credit for speculation purposes at all?

Mr. AYRES. They try not to.

Senator BROOKHART. And, second, they fix a wage for capital, an absolute wage and earning, so that there is no occasion for speculation?

Mr. AYRES. Yes.

Senator GORE. I did not get that last statement, Mr. Senator.

Senator BROOKHART. They fix a wage, an earning for capital, definite and arbitrary and absolute, which stays, does not vary up or down at all; and those things make for greater stability, do they not?

Mr. AYRES. Yes; they do.

Senator FLETCHER. Referring to Senator Wagner's inquiry about loans, I am curious to know whether or not this bill would correct that or not. We passed the reconstruction act to help organize them and we passed the Glass-Steagall bill to help them. Is it not a fact that generally throughout the country the banks are refusing to make loans and are calling in loans and making collections?

Mr. AYRES. I should hate to try to answer that question, because I have been trying to find out the answer to it, and the testimony is distinctly diverse. I suppose it must be true that conditions are diverse in various localities. I do know that there has been, and we all know there has been, a reluctance to lend in a great many instances and a desire to get loans paid down. Now, that is slackening, that is leveling out, and I hope we have about come to the end and shall travel in the other direction.

Senator FLETCHER. I had a good many letters to that effect from business people, complaining not only that banks are not granting loans, but they are calling in the loans, and this other suggestion came to me, whether or not, if you know that to be true, there is pressure being brought to bear by the Treasury and by the Federal Reserve Board on the banks to subscribe for Treasury certificates and help out the Treasury generally to take these securities, and that that is one reason why the banks are calling in their loans, in order to accommodate the demand of the Treasury. Do you know whether or not that is so?

Mr. AYRES. I should not believe, Senator, that that would have much weight behind it. I have never known of a case in which a bank demanded payments on loans in order to accumulate funds to buy Government securities. I should really doubt it very much.

Senator FLETCHER. Well, the banks constitute a very large market for these Government securities.

Mr. AYRES. Yes; very large.

Senator GLASS. Have you any information to the effect that many banks subscribe to the Government certificates with great reluctance?

Mr. AYRES. I have heard bankers talk in that sense. I suppose we all have.

Senator FLETCHER. Then, in that degree, the Treasury largely influences the banks, does it not?

Mr. AYRES. The Treasury, I will say, is under almost an insuperable pressure. It has got to sell its issues. It must sell them.

Senator FLETCHER. It puts banks, then, under pressure, too, does it not?

Mr. AYRES. I should not want to say that, but one might infer it.

Senator FLETCHER. The latent intent of that observation was to show that my judgment is not so far faulty when I want to divorce the Treasury from the Federal Reserve System and not have it dominated as it has done and is doing.

We are greatly obliged to you, Colonel, and I am sure the chairman is also.

Senator BROOKHART. Yes, indeed. We will recess now until 3 o'clock at the Interstate Commerce committee room, upstairs, at the Senate.

(Whereupon, at 12.55 o'clock p. m., a recess was taken until 3 o'clock p. m. of the same day.)

AFTER RECESS

The committee reconvened in the hearing room of the Committee on Interstate Commerce in the Capitol, at 3 o'clock p. m., at the expiration of the recess.

The CHAIRMAN. The committee will come to order. Mr. Wolfe, you may come around to the committee table and take a seat opposite the reporter. Please give your name, address, and business, and then you may proceed. But let me ask you first, how much time do you want?

Mr. WOLFE. It will not take me more than ten minutes to say what I have to say; depending upon how many questions may be propounded.

The CHAIRMAN. That is a very reasonable request. We are in a hurry to get along as well as we can. You may proceed.

STATEMENT OF O. HOWARD WOLFE, CASHIER OF THE PHILADELPHIA NATIONAL BANK, PHILADELPHIA, PA.; PRESIDENT OF THE ASSOCIATION OF RESERVE CITY BANKERS, VICE PRESIDENT OF THE PENNSYLVANIA BANKERS' ASSOCIATION, MEMBER OF THE ECONOMIC POLICY COMMITTEE OF THE AMERICAN BANKERS' ASSOCIATION, AND MANAGER OF THE PHILADELPHIA LOAN AGENCY OF THE RECONSTRUCTION FINANCE CORPORATION

Mr. WOLFE. In addition to what I have said I will add that just at the present time all of my time is taken up with the duties

of the Philadelphia loan agency of the Reconstruction Finance Corporation.

Senator COUZENS. I wish we might ask questions of the witness on that subject.

Mr. WOLFE. I shall be very glad to have you do so. In fact, I will refer to it if you will let me.

Senator COUZENS. I hardly think it is appropriate under this bill, though.

Mr. WOLFE. That may be. But I think I can show you how it is operating.

Senator COUZENS. Well, we will listen to you as you go along.

Mr. WOLFE. What I have to say, Senator Glass, is not the result of any prearranged notes or statement or anything of that sort. I have studied this bill very carefully, and this morning I listened to the testimony given before you with a great deal of interest, and I came to some conclusions.

But before I mention these conclusions I have arrived at, in regard to the bill, I should like, if possible, to have it appear on the record of your hearing that I was a friend of the Federal reserve act at a time when it needed friends. I had known Doctor Willis for many years, and during the time that bill was being constructed I was a paid employee of the American Bankers' Association and an officer of that association, and all the preliminary organization committee work was done in our offices of the American Bankers' Association at New York at Doctor Willis's request.

During that time I appeared before many of the bankers' conventions in different parts of the country in defense of the Federal reserve system. I was being paid by the American Bankers' Association at that time, which I think is rather conclusive evidence that the American Bankers' Association as such was not in any way opposed to the Federal reserve act as seems to be the general belief.

Senator GLASS. It is not only the general belief but the absolute record. And I should say that it was a very anomalous situation that one of the paid officials of the American Bankers' Association should be in favor of the Federal Reserve Act when the American Bankers' Association itself was against it.

Mr. WOLFE. Well, I will let Mr. Haas answer for that matter, but I do not think that is quite a correct statement.

Senator GLASS. I think it is.

Mr. WOLFE. During that period I originated and developed the gold settlement fund. That was my particular contribution to that work, and I, therefore, feel somewhat embarrassed here to-day by appearing in opposition to your bill.

Senator GLASS. Get it out of your mind that this is my bill. It is a bill made up by the Subcommittee of Banking and Currency of the Senate. It was introduced by me by the unanimous instructions of the subcommittee.

Mr. WOLFE. Well, I will proceed now with my statement.

The CHAIRMAN. Go right ahead.

Mr. WOLFE. I think it was the Senator from Kentucky (Mr. Barkley), perhaps, who asked Mr. Hecht the question whether in his judgment, this bill corrected our present weaknesses in the banking system. It seems to me that it does not, which is the chief reason I have at this time for offering, I might say, some criticism of it.

If the Members of this Senate committee could sit with me in the office of the Reconstruction Finance Corporation, at Philadelphia, for a week and examine the banks as we are obliged to examine them, I think they would agree with me that there is nothing in the bill, so far as I can find, except one thing, and that is at the end of the bill; that there is but one provision in this whole bill that in any way, in my judgment, would correct our troubles, and that is the very last paragraph of the bill.

The banks that are of the type that have been failing for the last two years are not at all touched by this bill, even remotely.

The banks that to-day are coming to the Government, we will say for assistance, coming to the Reconstruction Finance Corporation, I mean, are suffering from a multiplicity of troubles they have fallen heir to over the generations back to the days of free banking, when any person was permitted to go into the banking business. There is no restriction in the National Bank Act upon the directors, except that they shall live in a certain place, and nothing on the officers of any kind. That is the principal weakness in our banking system to-day.

Senator GLASS. And this would be a very opportune time to correct that.

Mr. WOLFE. I agree with you. You have done that in the last paragraph of this bill where you have permitted the Comptroller of the Currency to remove an officer for cause, which you could never do before. That is the really constructive measure in this bill.

Senator GLASS. I thought maybe that might be disastrous to the banking situation at this time.

Mr. WOLFE. No; I think it is a fine thing. I think most bankers would agree with my point of view in that matter, although I have talked to but very few bankers upon it.

The CHAIRMAN. You may proceed with your statement.

Mr. WOLFE. The trouble with banks to-day is that they make mortgage loans but they are not mortgages that are paid down at all. In other words, they are not installment mortgages. Some small banks are compelled to buy high-intesert-bearing bonds. They bought that class of bonds because they had to, to meet the expense. They have in their portfolios so-called commercial loans that are not commercial loans in fact; they are capital loans.

Senator GLASS. Ought they to be permitted to do that sort of thing?

Mr. WOLFE. No.

Senator GLASS. But this would be an unfortunate time to correct that.

Mr. WOLFE. I agree with you that—

Senator BROOKHART (interposing). Out in our section of the country they bought those bonds because the bank examiner said it was good banking.

Mr. WOLFE. That is true. But I am talking of the type of bond paying 6, 6½, and 7 per cent that we do not see so often; and they were bought on that basis, not liquid bonds, not listed anywhere, but 6 per cent bonds.

Senator BROOKHART. If they were liquid, they would be able to sell them on the stock exchange.

Mr. WOLFE. No; very few of them are listed bonds.

Senator BROOKHART. Those sold out in our section of the country were.

Mr. WOLFE. Then they were better than those offered in Pennsylvania. Lots of those bonds in the Pennsylvania banks are not listed.

Senator GLASS. You do not think any statute ought to restrain a bank from that sort of investment, do you?

Mr. WOLFE. You can not do it by statute. In other words, you can not make a banker good by statute. You can not make a bank strong by regulation.

Senator GLASS. Therefore, you think there ought to be no statutory restriction and no regulation for banks?

Mr. WOLFE. No, Senator Glass, that is not what I am saying. I am still talking on the last paragraph of the bill. I think we should keep out of the banking business men not capable of running banks. That is my first suggestion.

Senator GLASS. But you think we ought not to do that right now?

Mr. WOLFE. It would not do any harm to do that right now. That is one thing you can do right now without doing any particular harm.

Senator FLETCHER. Can you do it by legislation?

Mr. WOLFE. Yes; and you are trying it right here in this paragraph, this last paragraph of the bill, and very properly trying to do it here.

Senator GLASS. Would you repeal all the legislative restrictions in the national bank act and in the Federal reserve act that undertake to put a limitation upon the kinds of businesses that a national bank may engage in?

Mr. WOLFE. Not at all. But I am stating this fact, that a good bank needs no such legislation. For instance, you do not need to tell our particular bank, if I may use it as an illustration, that it must carry a reserve. We do not have a single mortgage loan in our shop. We do not think they are good for a bank to have.

Senator GLASS. But there are some banks and some bankers who do make those inadvisable loans.

Mr. WOLFE. Yes.

Senator GLASS. And should not they be restrained by regulation or by statute?

Mr. WOLFE. They are. But that does not necessarily make it a good banking system.

Senator GLASS. But it would be a pretty poor banking system without any restraints.

Mr. WOLFE. Yes.

Senator GLASS. If we have a poor banking system in spite of restraints, it would certainly be a poorer one to have no restraints.

Mr. WOLFE. Yes. But, Senator Glass, you do not get exactly what I am trying to say. I say in spite of the regulations we have had bank failures, and this present bill in my judgment does not go to the root of the trouble. In other words, the only kind of banks this puts any further regulation or restraint on are the strong and big banks that have not gone down, while the little banks that have gone down are not touched by this bill directly at all.

If you will let me illustrate that point: It would seem to be the theory that this bill is built up on (judging by the language used in the bill), that you should control collateral loans, and that is in the very language of the bill; that such loans may be speculative, whereas

unsecured commercial paper is not speculative, and yet the reverse might be true.

I think I can illustrate that to you by saying—

Senator GLASS (interposing). Speculative in the sense that commercial paper is not bought based on the minute or the hour. In other words, a man who makes a loan on commercial paper does not have to stand at a ticker and find out what is going to be the value of it 15 minutes afterwards.

Mr. WOLFE. Let me illustrate what I mean: A man came to my desk before I left the bank I am now with (I am with the Reconstruction Finance Corporation, temporarily loaned to that work); a man came to my desk and wanted \$10,000. I said to him: Let me see your statement. He showed it to me. He owned \$190,000 worth of good, well-secured bonds, listed bonds. I said: "We will loan you that sum of money if you will give us some of the bonds for collateral." He put up the bonds and got the loan. That was not a speculation on our part. Now, those bonds represented his surplus. He did not want to sell them. He got his \$10,000. He did not want to sell those bonds at that time because the market had depreciated. Now, if we had taken \$10,000 of unsecured paper it would not be as good as taking the collateral and—

Senator GLASS (interposing). The safety of a loan is not all of banking.

Mr. WOLFE. But it is a good part of it.

Senator GLASS. It is not all of it, however. Liquidity has a good deal to do with it. Do you mean to say there is no distinction between commercial banking and investment banking?

Mr. WOLFE. There is a great deal of distinction. Commercial banking is one thing, and investment banking is another thing.

Senator GLASS. One would suppose they should be, but they are not.

Mr. WOLFE. They are in good, well-managed banks, of which I am glad to say we have a majority in this country.

Senator GLASS. But we are trying to correct the evils of mismanagement of banks.

Mr. WOLFE. I do not think your bill does it.

Senator GLASS. That is a difference of opinion.

Senator FLETCHER. Mr. Wolfe, are you in favor of separating banking in its proper sense from going around and peddling securities?

Mr. WOLFE. Yes. And that has been done by some banks before this. Some banks gave up their affiliates when they saw the tendency. They did not need any law to make them do it. They did it themselves, and that is a matter of record. They just voluntarily gave over their affiliates.

Senator GLASS. As a matter of statement; yes. Some of these bankers came before our subcommittee and testified that they thought affiliate banking was a very vicious system of banking, and accepting the statement of banks to that effect, we have undertaken over a period of years by this bill to separate affiliates from commercial banks. Do you think that is a desirable thing to do?

Mr. WOLFE. That at the present time I am afraid will have a deflationary effect.

Senator GLASS. Well, we propose to give them three years to put their house in order. Do you think that is too limited a time?

Mr. WOLFE. If we were in a higher market right now for bonds, I should say you would not need three years. In fact, you would not need three months. But there is no assurance that they will be able to part with some of their securities within three years without suffering a great loss and further depressing the market.

Senator GLASS. And if we were in a higher market we would be told not to interfere with prosperity.

Mr. WOLFE. If I may go on with some concrete things that appear ill advised?

The CHAIRMAN. Proceed.

Mr. WOLFE. In the first place, I would suggest that that word "collateral" where it appears at so many places in the bill should be made more definite as to what it means. I have in mind suggesting—

The CHAIRMAN (interposing). One question right there: Does the word "collateral" in common practice mean the same thing in all sections of the country now?

Mr. WOLFE. I could not answer that question.

The CHAIRMAN. Or do bankers in the different sections of the country have different interpretations for it?

Mr. WOLFE. Let me read to you from the Reconstruction Finance Corporation act [reading]:

All loans made under the foregoing provisions shall be fully and adequately secured. The corporation, under such conditions as it shall prescribe, may take over or provide for the administration and liquidation of any collateral accepted by it as security for such loans.

Now, what do we mean by collateral? [Reading:]

Such loans may be made directly upon promissory notes or by way of discount or rediscount of obligations tendered for the purpose, or otherwise in such form and in such amount and at such interest or discount rates as the corporation may approve.

Now, we mean secured paper. What is secured paper? Mortgages, bonds, or anything put up as collateral under this act, and that is the interpretation that most bankers put on it when one says a loan is collaterally secured.

Senator BULKLEY. Is that the definition stated in the act itself?

Mr. WOLFE. No; that is not the definition.

Senator BULKLEY. Where does that definition come from?

Mr. WOLFE. The Chairman asked me what we considered to be collateral in a bank.

The CHAIRMAN. I did not ask that question at all.

Mr. WOLFE. Well, I will say—

Senator BULKLEY (interposing). Whose definition did you give us just now?

Mr. WOLFE. It is not a definition but a ruling of the Reconstruction Finance Corporation.

Senator FLETCHER. In circular No. 1?

Mr. WOLFE. I think it is No. 1.

Senator FLETCHER. And what do you see in this bill that is different?

Mr. WOLFE. Well, I will say that I read this reconstruction act over just once and I had a pretty clear grasp of it. But I have

read this bill over six times and each time I find something new, and I have had 33 years' banking experience.

Senator FLETCHER. Then you contend that we should define in our bill something that is not defined in the other act?

Mr. WOLFE. I do not mean that exactly, but if you leave it as it is here then very properly the Federal Reserve Board might say a warehouse receipt is a collateral which would fall under this act.

Senator FLETCHER. And I am inclined to agree with you on that point. But I wanted to find out how the other act was so much better drafted.

Mr. WOLFE. I would not say so much better drafted, but by collateral we mean anything put up as a loan.

Senator GLASS. We have asked bankers appearing before the committee to supply us with a proper definition and they have declined to undertake it. One witness, an exceptionally intelligent man from Kansas City, made that objection and we asked him to furnish us with language that would make it clearer and more explicit. And although he had been in the banking business for 40 years, five years longer than you have, he said he could not do it.

Mr. WOLFE. Very probably, judging by that answer, he did not know what you had in mind. I would have to know what you have in mind in drafting it.

Senator GLASS. I wanted him to indicate what he had in mind. We knew what we had in mind all right.

Mr. WOLFE. I think you mean stocks and bonds.

Senator GLASS. Yes. We do not mean commodities and warehouse receipts and things of that sort.

Mr. WOLFE. I am afraid you will get in a jam if you do not make it clear.

Senator GLASS. We won't get in any "jam" if the people who administer the law do not "jam" the law.

Mr. WOLFE. Now, there are just two or three other things and then I will have finished with what seems to me ought to be given consideration. One is a provision in the bill that—

Senator FLETCHER (interposing). Do you recommend that we define the word "collateral" there?

Mr. WOLFE. Yes.

Senator FLETCHER. To mean what?

Mr. WOLFE. To mean just what you want it to mean.

Senator FLETCHER. What would you say it should mean?

Mr. WOLFE. I would not want you to put me in the position of telling you what you mean, but I think you mean stocks and bonds. But you have not said so.

Senator FLETCHER. Do you mean all kinds of bonds?

Mr. WOLFE. Well, you take care of Government bonds in the next sentence.

Senator FLETCHER. You mean that we would have to define it if we did not want to exclude them.

Mr. WOLFE. Yes.

Senator GLASS. But we do exclude Government bonds.

Mr. WOLFE. I would say that you mean other bonds than Government bonds.

Senator GLASS. All right.

Mr. WOLFE. You have a provision in this bill in which you legislate against the purchase and sale of excess reserves. Now, I have been doing that in my own bank for a good many years. That has been my particular job for 15 years. I have been buying and selling excess Federal reserve funds. In that provision in attempting to fix the rate at which Federal Reserve funds should be sold you are running counter to ordinary business, which depends upon supply and demand.

If I may illustrate the point: Our particular bank is the fiscal agent of the State of Pennsylvania. Not long ago the State of Pennsylvania sold \$20,000,000 worth of bonds, and they deposited that \$20,000,000 with us as of a certain date. Under the laws of Pennsylvania, we are bound to begin paying interest on that deposit at once.

Of course you may say that we do not have to be a fiscal agent. I might go further and say, we do not have to be in the banking business. But we took the money, and we had to make it earn its way. The first thing to do was to get the State Treasurer to tell us when he would take the \$20,000,000. He said he could not tell us, that it might be a longer or a shorter time. I was forced to sell it day by day. In our own market I had to sell it at a lower rate than the discount of the Federal reserve act. We had to take care of it in that way until the Treasurer of the State of Pennsylvania took the money away, and then we no longer had those excess funds.

Senator BROOKHART. Who did you sell it to?

Mr. WOLFE. To our neighbors. We sold some of it to New York but the most of it our neighbors. And they paid us by giving us their cashier's check.

Senator GLASS. It has a tendency to put the reserves at a minimum.

Mr. WOLFE. Do you mean the rate?

Senator GLASS. Which privilege has been badly abused.

Mr. WOLFE. Then why not legislate against some particular abuse rather than have us all suffer. This is a perfectly legitimate business. I do not see how you can stop it.

Senator GLASS. Then, if we can not stop it, the provision of the law will be inoperative.

Mr. WOLFE. Well, I did not mean to say that you can not stop it, but I do mean I do not see why you should stop it. Personally, I have not seen any abuse of it in our State. There might have been an abuse of it in other places, but if so I do not know of it.

Senator GLASS. My information is that it has been badly abused.

Mr. WOLFE. Could not you legislate against that particular abuse without making all of us suffer?

Senator GLASS. Well, we might, but the time is said to be inopportune; so we are advised not to legislate against any abuses.

Mr. WOLFE. I do not think you mean just that, Senator Glass.

The CHAIRMAN. You may proceed.

Mr. WOLFE. Now, another matter here is this bill, and this is a question that has been taken up so many times: You propose to permit Federal reserve banks to loan at 1 per cent higher on 15-day paper. I want to say, Senator Glass, that I listened to Mr. Hecht's testimony this morning in which you questioned him as to eligible paper. And I want to say that it is a serious problem. Our own

particular bank is one of the largest commercial banks in the country, and has purchased for years more commercial paper than the average institution. Yet, owing to the fact that we had to loan other banks in order to keep them going some \$40,000,000, we were running perilously close to our limit. We loaned that money and we had \$70,000,000 of Government bonds on which to operate. If we had not been permitted to do that we would have had to cut down our loans to our correspondent banks right away in order to defend ourselves.

Senator GLASS. It is a special privilege, you know.

Senator BULKLEY. Of course, this bill would not prevent you from doing that.

Mr. WOLFE. It would cost us 1 per cent extra, and, therefore, we would have had to put that much more cost onto the country banker.

Senator GLASS. You might not have been forced to do it. You could rediscount.

Mr. WOLFE. And we did up close to the limit of our commercial paper, and with no more available what could we have done? And I do not know where we could have gotten more.

Senator BULKLEY. How do you reconcile that statement with the figures Senator Glass gave from the Federal Reserve Board?

Mr. WOLFE. I do not attempt to do it. But I question Senator Glass's figures.

Senator GLASS. They are not my figures. They are figures furnished me by the chief of banking operation of the Federal Reserve Board.

Mr. WOLFE. I know that the commercial paper in the country has been running down ever since 1918. That is a matter of record, too.

Senator BULKLEY. But you do not question that there are more than three billions of dollars undiscounted now, do you?

Mr. WOLFE. I do not know about that. All I know is about our own bank, which is one of the largest commercial banks in the East.

Senator BULKLEY. Do you mean to say whether there is any doubt about that statement being true?

Mr. WOLFE. Yes, I do; from my experience. I know where he got those figures.

Senator GLASS. If they are not correct, then they ought to get another chief of banking operations.

Mr. WOLFE. Let me say this to you—

Senator GLASS (continuing). And they were made up from reports of the member banks throughout the country.

Mr. WOLFE. And a lot of those banks put down what paper they have and call it commercial paper. But they have attempted to put that paper in at the Federal reserve bank and have been turned down, showing it was not commercial paper. I will say that my office happens to be in the Federal Reserve Bank of Philadelphia, and almost every day they bring paper up to me and say: We can not take this paper. As a commercial bank you can take it. These country banks list it as commercial paper, but when it goes in to the Federal reserve bank they turn it down.

Senator GLASS. Then the reports made to the Federal Reserve Board are worthless.

Mr. WOLFE. No, sir; I would not say that, but they must be taken at a considerable discount.

Senator FLETCHER. In other words, they may have that amount of paper but it is not eligible.

Mr. WOLFE. Yes, sir; that is it. They think it is eligible paper, but it is not.

Senator BROOKHART. After they discount a good deal there would still be a lot of it left.

Mr. WOLFE. It is in \$5 and \$10 lots. They loan on notes and say it is eligible, but the Federal reserve bank won't take it. It is too small.

Senator BROOKHART. It is not because it is not eligible, but because it is too small?

Mr. WOLFE. Yes, sir. And as a matter of fact, it is difficult to determine its eligibility. Say a borrower wants to borrow \$100, and then the bank can not use that paper without a statement.

Senator BROOKHART. Then we will have to amend this bill in order to treat the little fellows like the big ones.

Senator GLASS. Has there been an effort to create a market for commercial paper? Have the Federal reserve banks ever bought a dollar of commercial paper in open-market transactions?

Mr. WOLFE. I would not be prepared to answer that question. I never worked in a Federal reserve bank. They discount a lot of commercial paper, but I don't think they buy it in the open market.

Senator GLASS. Suppose this country had never entered the World War and you did not have United States bonds to use for 15-day loans, what would you do?

Mr. WOLFE. I think you would have to change the Federal reserve act. I do not think there is enough commercial paper to do the business we are doing. For instance, the merchant in the little country district does not store up his shelves with goods like he once did, on account of easy transportation.

Senator GLASS. It is not simply a matter of transportation, but the whole system of banking is being changed because corporations have come to be money lenders. They issue their securities and put them on the stock exchange and thereby accentuate the opportunity for gambling in stock instead of going to the banks.

Mr. WOLFE. Very well; how will you stop that?

Senator GLASS. We are undertaking to do that in the matter of loans to others.

Mr. WOLFE. But the banks did that long ago.

Senator GLASS. Not long ago.

Mr. WOLFE. As soon as the abuse became apparent.

Senator GLASS. The abuse has been apparent for years.

Mr. WOLFE. Only since 1929.

Senator GLASS. Not in such stupendous proportions as in 1929. Then the New York clearing house took action, I won't say because they saw it incorporated in a bill that I had drafted, but at any rate the New York clearing house adopted a regulation, which might be repealed to-morrow if they found it convenient.

Mr. WOLFE. The Philadelphia National Bank has always refused to make loans for others, and has followed that practice consistently.

Senator GLASS. I have no doubt there are good banks. But there are 22,000 banks in this country that are going concerns now; and when abuses enter the banking business, generally the only way we

can correct it is by a general statute or a general regulation and not by attempting to legislate for specific instances.

Mr. WOLFE. I think no one would say it is necessary to have a further act to prevent loans for others. I think most bankers are not engaging in that.

Senator COUZENS. If there is such a scarcity of commercial paper, why do you have to rediscount it in the case of a commercial bank?

Mr. WOLFE. If there is such a scarcity of commercial paper, why do we have to rediscount paper?

Senator COUZENS. Yes.

Mr. WOLFE. Well, I mentioned a while ago why we had—

Senator COUZENS (interposing). But not at this time?

Mr. WOLFE. We owed the Federal Reserve Bank \$40,000,000 a while ago, which was because country banks with whom we do business were sorely beset by depositors and were rushing out for help and came to us.

Senator GLASS. Why did they come to you?

Mr. WOLFE. Because there was nowhere else for them to go.

Senator GLASS. Why didn't they go to a Federal Reserve Bank?

Mr. WOLFE. Because they were not members of the system. Some are and some are not, but that was the situation.

Senator COUZENS. That does not answer my question. I am not talking about abnormal times when banks are closing and you have to come to the relief of a bank in order to protect your interests. Why, if commercial paper is going out, do you lay such stress on rediscount privileges in the Federal reserve system?

Mr. WOLFE. It is the best secondary reserve we have.

Senator COUZENS. Why do you use a secondary reserve when there is no great demand for commercial loans?

Mr. WOLFE. Because no bank could run without a secondary reserve.

Senator COUZENS. What kind of secondary reserve do you want to use?

Mr. WOLFE. Only commercial paper. It is the best kind we have. Bonds are not the best because you have to find a market for them.

Senator COUZENS. But you say you can not get commercial paper any more.

Mr. WOLFE. No; I did not say that.

Senator COUZENS. Well, you said you could not get an adequate supply.

Mr. WOLFE. Yes; for the present need.

Senator COUZENS. If the whole banking system is changed so that these commercial agencies that are benefited by the improved transportation facilities that you have referred to do not need to borrow, then just what do you mean that you want this money from a Federal reserve bank for?

Mr. WOLFE. I do not think I quite get your question, but we do not to-day have need for borrowing from the Federal reserve bank that we had six months ago. In the case of our own institution we have owed the Federal reserve bank nothing since the Reconstruction Finance Corporation came into being. I am speaking now for my own bank. But we always would like to have in our portfolio plenty of commercial paper so as to be prepared in case another need came along, a seasonal need, if you please. It would be a secondary

reserve that we could fall back on. I have not said there is not as much commercial paper, but not as much as Senator Glass's figures would make you believe.

Senator GLASS. Why do you speak of them as "Senator Glass's figures" when I have told you they are the official figures of the Federal Reserve Board?

Mr. WOLFE. Well, I beg your pardon, Senator Glass. I meant the figures you presented this morning.

Senator GLASS. I think they are accurate figures. I think they have better facilities for learning how much commercial paper there is in the country than you could have.

Mr. WOLFE. I think in our city the country banks use more paper in borrowing to-day than they did before. But the thing they call commercial paper is not commercial paper.

Senator FLETCHER. Are your loans increasing or decreasing?

Mr. WOLFE. Decreasing.

Senator FLETCHER. How much?

Mr. WOLFE. They are going down a great deal. Deposits are about stationary now, but they have been decreasing for a year or a year and a half.

Senator FLETCHER. Time deposits or demand deposits?

Mr. WOLFE. Both.

Senator GLASS. You say that the Reconstruction Finance Corporation has been a great help to your bank.

Mr. WOLFE. Yes, sir; not directly but indirectly.

Senator GLASS. Does that mean that the Reconstruction Finance Corporation is making loans to banks that you would not make?

Mr. WOLFE. No, sir. Well, it is making some loans that we would not make. For instance, we will not loan on real estate mortgages and they will.

Senator GLASS. Why won't you loan on real estate mortgages?

Mr. WOLFE. Because we are a commercial bank and want to keep ourselves much more liquid than would be the case if we had a lot of real estate mortgages.

Senator GLASS. That is what we provide for here in this bill, but it is inopportune to do that now, as I understand.

Mr. WOLFE. I would say so, sir.

The CHAIRMAN. You do not object to that provision in the bill, do you?

Mr. WOLFE. About mortgages?

The CHAIRMAN. Yes.

Mr. WOLFE. I should like to say that it was a great mistake when through force of circumstances you permitted national banks to take on mortgage loans. I do not think they have any place in a bank of deposit except it be an installment mortgage loan. That is my personal opinion, however.

Senator BROOKHART. As to this \$3,000,000,000 of available commercial paper, is that in member banks?

Senator GLASS. Yes.

Senator BROOKHART. It does not include country banks.

Senator GLASS. It includes all member banks of the system.

Senator BROOKHART. Isn't it true that country banks would add a good deal to it instead of subtracting from it?

Mr. WOLFE. Do you mean nonmember banks?

Senator BROOKHART. Yes.

Mr. WOLFE. I imagine so, but they can not put it up in the Federal reserve system.

Senator GLASS. Well—

Senator BROOKHART (interposing). I understand, but there is this much in the Federal reserve system.

Mr. WOLFE. It is so reported, which I question.

Senator BROOKHART. Then there are more banks outside the Federal reserve system than there are in it.

Mr. WOLFE. In numbers, yes; but not in size.

Senator BROOKHART. Those outside would have a good deal of commercial paper.

Mr. WOLFE. But that is absolutely useless because the provisions of the Federal reserve act preclude any bank loaning for some other.

Senator BROOKHART. Do you include that kind of paper in country banks?

Mr. WOLFE. No; in member banks, which report of commercial paper I am afraid, as to a considerable amount of it at least, is not really commercial paper. They so list it in their reports but an actual test would show that it is not commercial paper.

Senator GLASS. Well, of course I can not tell nor can this committee tell as to that. We are not charged with the business of discriminating.

The CHAIRMAN. I am very glad to have you clear up the point that the figures do not include all banks.

Mr. WOLFE. No; they do not.

The CHAIRMAN. They just include member banks.

Mr. WOLFE. Yes, sir.

The CHAIRMAN. But your statement awhile ago was that it included both?

Mr. WOLFE. No.

The CHAIRMAN. And you put emphasis on the nonmember banks?

Mr. WOLFE. No, sir.

The CHAIRMAN. They are separate and apart?

Mr. WOLFE. Yes, sir.

The CHAIRMAN. In other words, it is a case of addition instead of subtraction.

Mr. WOLFE. Yes, sir. All I want to say on that subject is that I suspect, having seen the inside of a large number of country banks, that a lot of the paper listed by the Comptroller of the Currency as eligible is not eligible paper.

The CHAIRMAN. All right. The eligible paper that Senator Glass has given is what figure?

Senator GLASS. It is \$3,069,000,000.

The CHAIRMAN. And the rediscount is what?

Senator GLASS. In addition to the \$3,069,000,000 of commercial paper, the report was that \$5,500,000,000 of governments were usable for rediscount purposes, and the total discounts of the Federal reserve banks at that time was considerably less than half a billion dollars.

The CHAIRMAN. In other words, the figures, if he took a discount at 50 per cent off the Federal reserve, would still leave an astounding amount of available paper.

Mr. WOLFE. What happened was this: Very frequently, this country being so large, while the Southwest might have plenty of commercial paper, the eastern section of the country might not have it; and you would have in total figures a tremendous amount available and yet it is not in the right place, and there is no way to get it there.

Senator GLASS. The report of the chief of banking operations of the Federal reserve system showed a pretty even distribution of commercial paper.

Senator FLETCHER. Do you regard the Federal reserve banks as being very strict in their classification of what is eligible paper and what is not?

Mr. WOLFE. The interpretation is put on rather by the individual bank. In other words, paper comes to a Federal reserve bank for rediscount and they say yes or no. Of course, the Federal Reserve Board lays down broad general principles. Having sat in on the interpretation of the act, I remember with what particular care Doctor Willis tried to find out a satisfactory definition of eligible paper, and am quite sure he was never able fully to satisfy himself on that point. When paper is presented to Federal reserve banks, they decide without asking the board. I am confident that some banks may be more strict than others.

Senator GLASS. If you think you wrote the Federal reserve act, then I have been laboring under a delusion for 18 years; and if the American Bankers' Association favored the Federal reserve bank system, I wonder why on earth I took the whole legislative committee of the American Bankers' Association, composed of Sol Wexall, George M. Reynolds, Festus Wood, Mr. Forgan, and four or five others up to the White House to prevail upon the President to have a good many of its features changed. I wonder also why the American Bankers' Association in its annual convention at New Orleans unanimously, or I believe with one dissenting voice, indorsed the Aldrich bill instead of the proposed Federal reserve bill. And why the American Bankers' Association in its group meetings and in its convention at Boston just a few weeks before the Federal reserve bill became a law, declared against it. I have been totally misinformed about these events if your statement is correct; I have just been deluded for the past 18 years.

Mr. WOLFE. Senator Glass, I don't think you quite want to get it in the record that I said I wrote the Federal reserve act, do you?

Senator GLASS. No.

Mr. WOLFE. Do you think it quite fair that it should go down in the record that way?

Senator GLASS. You certainly said here that the American Bankers' Association was in favor of it.

Mr. WOLFE. I did not say that. I said they were not unanimously against it. I said I also happened to know about—

Senator GLASS (interposing). Well, the record will show what I said.

Mr. WOLFE. But the record won't show that you said what you said with a smile.

Senator GLASS. Maybe not. Well, in that case I will try to adopt a different type of smile. I have been accused of talking out of

one side of my mouth, but I didn't know I was accused of talking with a smile. I will see if I can adopt my smile to circumstances.

Mr. WOLFE. I have nothing further to say unless the members of the committee want to ask me some questions.

The CHAIRMAN. Mr. Wolfe, are we to understand that you have no objection to the other provisions in the bill except what you have said?

Mr. WOLFE. There are some minor things, but I have enough confidence in the intelligence of this body and in the intelligence of the Senate to realize that you and they will correct some of the little minor things I might call your attention to. It seemed to me that the major thing was to do something to correct the weak situation of the small country banks. That is our principal danger, and it may be that you can do nothing to correct that situation.

The CHAIRMAN. I live in a country of weak country banks, and when a bank went down I was told we could do nothing. But I now see the same trouble has overtaken you people in the East, and now it seems to be something different.

Mr. WOLFE. You will find in section 29 of the bill one constructive thing to correct the situation, namely, to try so far as you can to keep out of the banking business men not qualified to be in it.

The CHAIRMAN. One of the most notorious failures we had was a big bank for \$200,000,000 in deposits.

Mr. WOLFE. Yes; but that was only one out of thousands

The CHAIRMAN. It involved four times over the total money in bank failures in certain States.

Mr. WOLFE. Yes; but the New York banking department could not get those men out of business because they did not have this kind of law.

The CHAIRMAN. But the big banks seem to go with the small banks. That was a branch-banking system that is so highly recommended now.

Senator BROOKHART. I will say that I was in Louisville, Ky., when the \$57,000,000 National Bank of Kentucky went up.

Senator GLASS. Let me read for the record and for your information, if you are willing to believe it, Mr. Wolfe, the official statement as of this month, March of 1932, from the Federal Reserve Board, as appears in its official bulletin. [Reading:]

The need for this legislation has not arisen from shortage in the aggregate amount of the assets held by member banks. At the end of December they reported they held \$2,573,000,000 of eligible paper in addition to \$1,694,000,000 of Government securities, or a total of nearly \$7,300,000,000, exclusive of Government bonds pledged as collateral for national bank notes. These figures would seem to indicate that the amount of eligible assets in the possession of member banks of the Federal reserve system is nearly ten times as much as their aggregate borrowings from Federal reserve banks. These eligible assets furthermore are fairly well distributed throughout the country among the member banks, so that the number of individual banks that are not in a position to borrow to some extent on eligible paper or Government securities is relatively small.

Of course, that report is three months later than the report I referred to a while ago.

Senator TOWNSEND. Mr. Wolfe, from your study of the provisions of this bill, do you think it would help the Federal reserve banks, that is, the country banks, to come into the Federal reserve system?

Mr. WOLFE. I am afraid it would have a tendency in the opposite direction, but that is merely my opinion and I may be entirely

wrong, and will hope that I am. As a matter of fact, I believe we ought to force into the Federal reserve system, if we can, every bank that does a commercial business, whether State or national bank. But I do not see how we could do it.

Senator TOWNSEND. I was hopeful that the bill would so attract the country banks that they would be anxious to come into the system.

Mr. WOLFE. I am afraid not. I happen to know two State banks that came in as a patriotic measure, but have never used the Federal reserve at all. Both say they will go out under these circumstances.

Senator GLASS. Nearly all national banks, for that matter, said they would not come in; didn't they?

Mr. WOLFE. A good many said that, but they did not mean it.

Senator GLASS. Oh!

Senator BULKLEY. Then we have to discount that a great deal more than the figures Senator Glass gave.

Senator GLASS. If I had the file of the Boston Transcript for October of 1913, and I wish I had it here, I should like to read to you the vicious statement made by Mr. Hepburn, the banking scholar of the United States as of that time and chairman of the legislative committee of the American Bankers' Association, in which he said that the adoption of the Federal reserve bill would wreck the national-banking system, and yet in a little more than a month afterwards the first letter of congratulation, almost extravagant in its praise of me, was from Mr. Hepburn.

Mr. WOLFE. I will match that if I can: The then president of our bank, who was on that commission, told me the gold settlement fund would wreck the banks of the country. He was wrong.

Senator GLASS. When gentlemen come here and threaten us with a torrent of withdrawals from the banking system if we undertake some conservative reformation of abuses, we ought to take their threats with some degree of allowance.

Mr. WOLFE. I should say so. I do not want to go into the record that I am in any way opposed to the Federal reserve system or that I ever was at any time.

Senator GLASS. Well, I did not exactly identify you as the American Bankers' Association.

Mr. WOLFE. You have scolded me about what they did.

Senator GLASS. Well, I fear you got the wrong slant on my smile.

Mr. WOLFE. All right.

The CHAIRMAN. Is that all?

Mr. WOLFE. Yes; Mr. Chairman, I thank you.

The CHAIRMAN. We will now have Mr. McQuaid, president of the Barnett National Bank, of Jacksonville, Fla.

STATEMENT OF W. B. MCQUAID, PRESIDENT OF THE BARNETT NATIONAL BANK, JACKSONVILLE, FLA.

Mr. MCQUAID. I expect I better begin by reading my memorandum on this bill.

Senator FLETCHER. You have examined the bill, S. 4115?

Mr. MCQUAID. Yes, sir.

Senator FLETCHER. You may make any statement about it you like.

Mr. MCQUAID. I might say that while the bank of which I am president is in a reserve city, yet banks of our size are more or less

considered country banks by the metropolitan banks. Further, I will say that we have affiliate banks in the smaller towns in Florida; and the same thing is true of the two other large national banks in Jacksonville. Those banks were organized after the failure of banks in other cities, in order to supply some banking facilities where there were then no banking facilities at all in a good many instances.

I should like to present here just the view of how some of the provisions of this bill would affect the smaller banks, and particularly affect the communities which they serve.

We are all heartily in accord with constructive and sound provisions that may improve the present banking laws. The bill we have gone over is very drastic in a great many respects and would result in far more harm than good and would ultimately force a great many banks out of the national banking system. The subcommittee apparently had two principal objectives in mind: to curb loans by all banks on all classes of securities other than Government and municipal bonds and to curb or restrict the operation of corporations, which, under the definition in the bill are termed affiliates, and in incorporating their ideas of the remedies in the bill they have failed to realize the effect upon the general banking structure of the country, and particularly the effect upon country banks outside of the cities in which security markets are maintained.

Now, as to investment securities: Under the provisions of section 15 a bank may purchase for its own account only such investment securities as may be by regulation prescribed by the Comptroller, but in no event shall the total amounts held for its own account exceed 15 per cent of that bank's capital and 25 per cent of its unimpaired surplus. It has been common practice for banks to maintain a secondary reserve in Government bonds and high grade investment securities. The fact that banks have had tremendous losses due to depreciation in market values of such securities does not mean that securities of the highest grade and of reasonably short maturity are not still a sound investment for banks. Even United States Government securities have declined within three months as much as 16 points. The greatest security loss to banks has resulted from the purchase of low-grade domestic and foreign bonds, bought for the high return they gave or because of inexperience in the selection of securities. Restriction as to rating would have avoided the greatest part of this loss. The restriction as to amount of investment securities that may be held is a very drastic provision and will force banks into the investment in the less liquid municipal bond in investing time deposits.

Senator BULKLEY. Might I ask what section you now refer to?

Mr. McQUAID. Section 15. A bank is limited to the amount of investment securities it may purchase for its own account to 15 per cent of the capital and 25 per cent of the unimpaired surplus, not including United States Government bonds.

Senator BULKLEY. You take that to mean that a bank could not hold any more securities than that limit?

Mr. McQUAID. That is right.

Senator BULKLEY. In the aggregate?

Mr. McQUAID. Yes.

Senator BULKLEY. I do not blame you for that misunderstanding, but as a matter of fact this means that you can not hold more than that amount in one issue. That would quite change the situation, wouldn't it?

Mr. McQUAID. The limitation of the total amount?

Senator BULKLEY. No; but to the total amount of any one issue.

Mr. McQUAID. Well, I have no objection to that.

Senator BULKLEY. I thought you would not. I do not criticize your misunderstanding of the provision.

Senator GLASS. No; I think it needs to be clarified.

Mr. McQUAID. Well, that was my understanding of it.

The CHAIRMAN. Well, you may now go to your second objection. That objection we will meet satisfactorily when we come to write the bill.

Mr. McQUAID. I thought it was the total or aggregate amount.

The CHAIRMAN. You are not the only one who misunderstood the intent of that language.

Mr. McQUAID. Now, as to savings deposits or time deposits: The commercial banks outside of the larger cities almost invariably maintain savings departments. In a great many States there are but few strictly savings banks. Savings deposits and other time deposits probably represent 35 to 40 per cent of the total deposits of the national and State banks outside of the central reserve cities.

I have not the figures of the Comptroller of the Currency on that. I think I saw some recent figures wherein the demand deposits of member banks were approximately \$15,000,000 and time deposits of member banks were approximately \$11,000,000, but I don't know whether they are correct or not. However, that would not be uniform throughout a great number of banks. A great many banks do a very small business in savings deposits. Our savings deposits are not over 25 per cent of our total deposits.

Under the provisions of section 14 it is required that these deposits be invested in certain kinds of loans or in certain kinds of securities and that the banks report these investments when such reports are required by the comptroller. The investment of these time funds in real-estate mortgage loans, in unsecured loans whose eventual safety depends upon the value of real estate, and the investment in bank premises is approved to a total amount not to exceed half the bank's total time deposits.

Particularly in the country districts a great many loans are made to farmers and individuals whose wealth is largely represented by real estate. In a great many instances these loans are not made upon mortgage, since the borrower only needs the loan for a short period of time and it is not intended the loans shall run for a year or longer, but they must be considered under the terms of this act as real-estate loans and be kept within the limitations. Due to the automobile and good roads, the business life of the small city has changed materially in the last 15 years. The amount of strictly commercial paper eligible for discount with the Federal reserve bank which the bank in the small city can make is very limited.

The limitation on the amount of mortgage loans which may be made is proper, since such loans run usually from one to five years, but to include in this limitation open loans made for short periods whose eventual safety depends upon real property will severely

restrict the borrowing capacity of the community in which the smaller bank operates, particularly in agricultural districts where farm lands and other real estate in the principal basis of all loans. It should be permissive and not mandatory that unsecured loans whose eventual safety depends upon the value of real estate be counted for the purposes of section 14 as real-estate loans.

We have one bank that has not as much as \$100,000 of time funds. It has agricultural territory around it, and a great part of the loans it makes are advances to growers of citrus fruits, and other advances for agricultural purposes. They may or may not take a crop lien. The basis of those loans after all is real estate. There are professional men in that community, and there is a university in that community. Those men have definite incomes. They have property of one or two classes: It is either real or personal property. If they do not happen to have stocks or bonds it is real property.

They may come in to borrow some money for a short period of time, and the loan would be made based upon their income whether from real property or from a profession, but because their main estate is real estate that has to be classified as a real-estate loan. And if the bank should happen to have a small amount of time deposits, the amount of such loans the bank could make under the provision of this bill would be very limited, and the occasion will arise when some one will come in justified in expecting the bank to make such a loan.

Senator GLASS. What did you do when the law prohibited the making of any loans at all on real estate?

Mr. MCQUAID. We don't make them now.

Senator GLASS. Well, then, how do the provisions of this bill affect you if you do not make them now?

Mr. MCQUAID. Because under the provisions of that section of the bill, whether secured by real estate or not, if the ultimate safety of the loan depends upon real-estate values, they are classified for the purpose of that section as real-estate loans, and it says they shall not exceed 50 per centum of the time deposits.

I know of banks in a good many sections of the country that have taken advantage of the provisions of the Federal Reserve Act which permits them to loan money on real estate, but it has not been our policy to do that.

Senator TOWNSEND. Will you tell me where you find that in the bill?

Senator FLETCHER. It says at line 17, page 33, of the bill [reading]:

Investments in bank premises and unsecured loans whose eventual safety depends upon the value of real estate shall be counted for the purposes of this section as real-estate loans.

Senator TOWNSEND. Now, you want to change the word "shall" to the word "may."

Mr. MCQUAID. Yes; to me that would be better.

The CHAIRMAN. On what line is that?

Senator FLETCHER. It is on line 19. Then it would read:

Investments in bank premises and unsecured loans whose eventual safety depends upon the value of real estate may be counted for the purposes of this section as real-estate loans.

The CHAIRMAN. What would it mean if you changed the word "shall" to the word "may"? Who would have the discretion?

Senator TOWNSEND. The examiner or the Comptroller of the Currency.

Mr. McQUAID. No. The result would be that in reporting it would permit the bank to report as loans made for account of savings deposits up to 50 per cent of the time deposits, such unsecured loans as would be considered real-estate loans under this section.

The remaining 50 per cent of a bank's time deposits shall be invested under section 14 in securities in which savings banks of that State may invest; or, in the absence of State law, in securities to be specified by the Comptroller of the Currency. And because of my misunderstanding of the aggregate amount covered by this bill, the balance of my statement on that subject as I have it prepared would be incorrect, and I will not read it. I thought we were limited to the total amount and that that would force us then into the purchase of a less liquid investment, that is, a municipal bond, which has a very narrow market.

Now, as to loan restrictions: Section 8 provides that six members of the Federal Reserve Board shall have power to fix the percentage of each individual bank's capital and surplus which may be represented in loans secured by collateral. The board is given power to direct a bank to refrain from further increase in its security loans for a period up to a year under penalty of suspension of its rediscount privilege; and, under section 11, if member bank increases its outstanding loans to any borrower, with or without collateral security, for the purpose of carrying investment securities (except United States Government bonds) during the time the member bank is borrowing from the Federal Reserve Bank, its note immediately becomes due and payable, and it shall be ineligible to borrow on its 15-day note at the Federal Reserve Bank.

Shall six members of a board in Washington be permitted to set an arbitrary percentage of capital and surplus which may be loaned on collateral irrespective of the location of the bank and local conditions; to apply to all sections of the country or even to districts? There are over 7,000 national banks and State banks that are members of the Federal reserve system to which this would apply. It would be impossible for any board to know the purely local requirements for such loans in individual localities. Shall an individual borrower be denied a loan for legitimate purposes when he may have owned the securities outright for years, or the bank be denied the right to take any collateral and even the most marketable collateral for a loan for legitimate purposes or purely local needs and having no bearing upon speculation, just because the bank is then a borrower at the Federal reserve bank or its total loans secured by collateral of all kinds have reached a limit fixed for it by a board? What bank would not take collateral, when they can get it, in preference to making open loans? How is it possible for any board to differentiate between many loans made by an individual bank for perfectly legitimate business needs secured by market collateral and those made for purely speculative purposes? Shall we unduly restrict legitimate loans for fear a few speculative ones will slip through?

The term "collateral" there would apply to other things than market collateral. While we are not in the cotton section, yet we are in the naval stores section where such products as turpentine and resin will be stored in warehouses at the port, and the banks loan against those commodities. Furthermore, banks loan against another agricultural commodity, canned grapefruit, in my section of the country. We may loan against several other kinds of commodities, but these are all collateral loans to which this section would apply.

The CHAIRMAN. I should like to ask this witness a question the other witness did not answer: Is there a different meaning given to the word "collateral" in different sections of the country? In other words, would bankers have exactly the same thing in mind in reference to the word "collateral" in Jacksonville as they would have in New York?

Mr. McQUAID. In some places I think the word "collateral" should be more definitely defined.

The CHAIRMAN. It is not a definitely understood word at the present time, is that it?

Mr. McQUAID. Yes.

Senator GLASS. You would not call tomatoes or canned goods or citrus fruits collateral, would you, in the general accepted parlance of the banking business?

Mr. McQUAID. Well, Senator Glass, it says if you increase your loans on collateral.

Senator GLASS. I say, you would not call these commodities collateral?

Mr. McQUAID. Yes; while you are borrowing at the Federal reserve bank on 15-day loans.

Senator BULKLEY. Well, would you consider canned grapefruit or tomatoes as collateral?

Mr. McQUAID. Yes; if they are put in a warehouse the receipts are collateral.

The CHAIRMAN. But it may not be so considered in every section of the country; is that your understanding?

Mr. McQUAID. Generally, it is so considered. And they loan on receipts for wheat. That is collateral. They loan on warehouse receipts for cotton. That is collateral.

The CHAIRMAN. Are you afraid the way this bill is drawn it would exclude that?

Mr. McQUAID. It would prevent it at a time when we are borrowing from the Federal reserve bank, when we are making any additional loans on any form of collateral if we had reached the limit set by the board in Washington. Then the banks in our section of the country would have to turn down such loans or be subject to the penalty of being unable to use the rediscount privilege of the Federal Reserve Board.

Senator TOWNSEND. In the Tri-States it is very generally accepted that canned goods will be taken as collateral, or that receipts therefor are accepted.

Senator GLASS. I would call it security, but I would not call it collateral security.

Senator BROOKHART. That is a matter that can be easily corrected in the bill if it is found desirable to do.

Mr. McQUAID. I think it goes a little bit beyond that. For instance, it comes right back to the same thing I mentioned a while ago in reference to the limitation of loans; that the man not in commercial business may have some temporary need for money. He carries a good account at the bank; he has some bonds; instead of accumulating real property he is accumulating some personal property in either stocks or bonds, and he comes in and wants to borrow money on those bonds. The same thing would apply to that. We do not want to turn him down, but we would have to. We would have to say to him, "No; we have reached the limit that the Federal Reserve Board says we can lend on collateral, and you can not get it."

So he will go over to the State bank and negotiate.

The CHAIRMAN. You may proceed.

Mr. McQUAID. What really created a dangerous situation during the market boom was the large amount of money loaned by banks in the cities where security exchanges are operated to brokers for the account of "others." Money of corporations and individuals in all parts of the country.

The provision that a bank shall not act as agent of a nonbanking corporation in making loans secured by market collateral for their account is ample safeguard against large sums being loaned in the future for speculative purposes.

Very few banks will borrow or rediscount at the Federal reserve bank to carry what are known as "street loans," or loans to a non-customer of the bank, usually a broker, to carry market securities.

There were some violations of that during the 1929 market conditions, but I think they were comparatively few; that as a rule the banks would not borrow from the Federal reserve bank in order to loan that money on the Street.

Senator GLASS. There is nothing in this bill that prohibits the bank from loaning the money on the street. It can loan every dollar of its depositors' on the street, but there is an inhibition against coming to the Federal reserve bank and recouping itself after it shall have done that, particularly if it persists in extending loans of that kind.

Mr. McQUAID. Yes; but you see, Senator, when you put that limitation on there about increasing your loans on collateral, collateral of whatever nature, while the intention there is to prevent you from using the Federal reserve funds that you get and loan them for speculative purposes, in actual practice it is going to hit at your local loaning of that money.

Senator BULKLEY. Suppose the word "collateral" in there is to be read to mean what Senator Glass says it means: Then you do not have the same objection to it, do you?

Mr. McQUAID. It will not apply quite as harshly.

Senator BULKLEY. Regardless of that, is it not a sound restriction? There are lots of restrictions that are not entirely convenient to the party restricted, but they are nevertheless sound and wholesome in the long run.

Mr. McQUAID. The point I was making, Senator, was this: Suppose you were not in commercial business and a bank was borrowing from the Federal reserve bank on its 15-day note and you had bonds that you wanted to offer to the bank and you were not borrowing the money for speculative purposes at all, bonds in which

you invested your money some time ago. That bank could not loan you that money under those conditions.

Senator GLASS. Yes; it could, unless it appeared that the bank was loaning for speculative purposes, and loaning excessively. Thereupon that bank would be warned by the Federal reserve bank or board that its loans on speculative collateral were excessive and that if they continued to expand loans on speculative papers it could not get rediscounts at the Federal reserve bank on its 15-day notes. Is there anything unreasonable about that?

Mr. McQUAID. Well, but, Senator, you first say in the bill that that board shall fix the percentage.

Senator GLASS. It has the unlimited right now, has it not, to fix the percentage? You are talking about investing the board with power.

Mr. McQUAID. Yes.

Senator GLASS. Under the existing law it has an unlimited power to fix the percentage at anything it pleases, has it not?

Mr. McQUAID. Fix the percentage of loans that we may make on collateral?

Senator GLASS. No, the percentage; you are speaking now of the 1 per cent?

Mr. McQUAID. No, no.

Senator BULKLEY. Percentage of loans on collateral?

Mr. McQUAID. Yes.

Senator GLASS. No.

Mr. McQUAID. This bill gives them the right to fix the percentage of the loans which we may make on collateral, you see.

Senator GLASS. Oh, yes.

Mr. McQUAID. You come in then with your bonds.

Senator BULKLEY. Yes.

Mr. McQUAID. I say, "I have got to turn you down. You have carried an account with me for years, carried a good account."

Senator BULKLEY. I do not see anything very bad about that, if you haven't got any money to lend.

Mr. McQUAID. I think it has been a sound banking principle, and that is what the Federal reserve bank was put here for; that it was for the accommodation of business, commerce—

Senator BULKLEY. Yes, within sound limits; but it has not been for the purpose of giving you money to go ahead and loan more than you should.

Mr. McQUAID. If it is necessary to accommodate your local customers for legitimate needs, that you should use the Federal reserve bank for that purpose.

Senator BULKLEY. Not when you have got limitations on making loans that are not for such legitimate needs.

Senator COUZENS. Would you say that any specific amount could be fixed to regulate that?

Mr. McQUAID. The Federal Reserve Board fixes that amount; I do not know what amount is going to be fixed.

Senator COUZENS. Would you prefer the Congress to fix that amount rather than leave it to the board?

Mr. McQUAID. I do not believe an amount should be fixed.

Senator COUZENS. You do not believe any amount should be fixed?

Mr. McQUAID. No.

Senator COUZENS. You think you should lend all your money on that security then at the Federal reserve?

Mr. McQUAID. How can the board determine for me and 7,000 other banks what our particular local needs are, irrespective of any speculative conditions?

Senator COUZENS. Then your theory is that the bank can loan all its money on stock exchange collateral and to these brokers and investment houses without any restrictions at all? Is that your idea?

Mr. McQUAID. I do not think any limit should be fixed. But the banks are not going to do that.

Senator COUZENS. If they are not going to do it, just tell us where they are going to stop at.

Mr. McQUAID. Well, Senator, I do not believe that any legislation should just so closely define what a bank shall and shall not do as to let that entirely take the place of management and judgment in the operation of a bank.

Senator COUZENS. No.

Senator GLASS. Haven't they done it 40 times in the national bank act and here in the Federal reserve act?

Mr. McQUAID. You have put certain broad limitations on, Senator.

Senator GLASS. We have put many specific limitations upon it.

No member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm or corporation, to an amount equal at any time in aggregate more than 10 per cent of its paid up and unimpaired capital stock and surplus—

And so forth.

The Federal Reserve Board under such general regulations as it may prescribe, which shall apply to all banks alike, regardless of the amount of capital stock and surplus, may authorize any member bank to accept such bills to an amount not exceeding at any time in the aggregate 100 per cent of its paid up and unimpaired capital stock and surplus—

And so on and so forth, all through the act, limitations occur and authorizations occur.

The Federal Reserve Board and Federal reserve banks are empowered by general regulation to put limitations upon certain classes of loans in stated percentages. You would strip the board of all that power, would you?

Mr. McQUAID. Senator, is there any place in there now where there is a limitation on the total aggregate amount of loans of any class that a bank may take except real-estate mortgage loans?

Senator GLASS. No; and that is the reason we are trying to put it in now. But I am speaking of the relative authority of the board. There have been protests against confiding certain authority to a central board here, and we have over and over and over again, both in the national bank act and in the Federal reserve act, confided such authority either to the Comptroller of the Currency or to the Federal Reserve Bank or Board.

Mr. McQUAID. Of course, this is only one kind of loan. A bank may make a classification of its loans for its own purpose to see that it gets a proper distribution of loans.

Senator GLASS. Can you cite us to any abuses of authority in circumscribing loans of which a Federal reserve bank or Federal Reserve Board have been guilty?

Mr. McQUAID. Not yet; no.

Senator GLASS. I can cite you to some expansion of loans where they have been very guilty.

Mr. McQUAID. They have been liberal in their views, I understand, sometimes.

Senator GLASS. I think that is what is the matter with the country to-day. You see, you require six members of the board to agree. Do you think it is reasonable to suppose that you could get six members of the Federal Reserve Board to adopt a regulation that would operate harshly upon a great many banks? The board, we naturally assume, wants to facilitate business transactions, wants to see them expand legitimately in an unrestricted sense. Do you think it would be reasonable to suppose that you could get six out of the seven members of the board to adopt a regulation that would work a great hardship upon any number of banks?

Mr. McQUAID. Why, I suppose that the board you would have in the future would be just as good as the board you have had in the past, and that they would all be reasonable men. At the same time, can you fix a percentage for collateral loans to be made in all sections of the country, all banks? There may be different requirements in different sections at different times of the year.

Senator GLASS. My guess is that if they were to exercise that authority they would exercise it in a rather too liberal way than in a restrictive sense. That would be my guess.

Mr. McQUAID. Well, you see the importance of at least more particularly defining the word "collateral."

Senator GLASS. I think it might be more comprehensively defined, though I confess I would not know exactly how to do it, and some very experienced bankers who have testified here have said they would not know how to do it. I know just exactly in what sense we use the term there, and I do not think it relates to such transactions as you have enumerated.

Mr. McQUAID. Reserve requirements: The present legal reserve required to be carried with the Federal reserve bank is only a part of the cash a bank has to have to conduct its business. This legal reserve with cash in value and in balance with correspondent banks will run on an average 20 to 25 per cent of its deposits. This is unproductive of any revenue except the small amount of interest it receives on the balances with correspondent banks in reserve cities. The bill increases the reserves required on time deposits to a fixed rate. After a study of a year by the Federal Reserve Board, a far better method of reserve requirements has been suggested, which would automatically increase the reserve requirements in times of increasing activity occasioned by either speculative or business boom conditions and thus act as a brake on excesses.

Senator GLASS. You are for the immediate adoption of the velocity system, then, are you?

Mr. McQUAID. Yes, sir.

Senator GLASS. Do you think it would be thoroughly understood throughout the banking community in the United States?

Mr. McQUAID. They have to learn it.

Senator GLASS. We do not want to do anything now that anybody has got to learn.

Mr. McQUAID. There will not be much change in the velocity for a while to come yet.

Senator GLASS. The suggestion that we make here is a pretty slow process. It extends over a period of five years and merely restores the reserves to where they were when we reduced them last. So I do not think there will be much velocity in the system for some time to come, certainly not if anybody will read the hearings we have had here in the last three or four days.

Mr. McQUAID. Liquidation Corporation: Section 12 "B" provides for a corporation which may purchase the good assets of a closed bank in order to give quick relief to depositors and provides that member banks shall subscribe to Class "A" stock of the corporation equal to one half of one per cent of their total deposits. This corporation is plainly not to make any profit on the assets of a closed bank. The interest the corporation receives on its invested capital funds and the liquidation fee will hardly do more than pay its operating expenses, and the member banks may expect no dividend on their Class "A" stock. Why should we be forced to contribute to the capital of such a corporation? The member banks now, by the reserves they carry with the Federal reserve banks without any interest, and their subscription to its stock, supply the funds with which the Federal reserve banks make their profits. The profits of the Federal reserve banks above dividend requirements alone should be used for this purpose, supplemented by that part of the appropriation made to Reconstruction Finance Corporation for the same purpose.

Senator GLASS. Did your bank contribute to the National Credit Corporation?

Mr. McQUAID. We are already contributing through the Federal reserve bank. Now we are asked to take in addition to that stock—

Senator GLASS (interposing). No; but I say, did you contribute to the National Credit Corporation?

Mr. McQUAID. No, sir; we did not.

Senator GLASS. Did not want to, did you?

Mr. McQUAID. Didn't think well of it.

Senator GLASS. You had not been apprised of the fact that the people who were engineering it had been promised here in Washington that it would be taken over at the expense of the taxpayers of the country, did you?

Mr. McQUAID. I did not know there was any promise made to that effect.

Senator GLASS. Well, it is of record here that there was.

Mr. McQUAID. In the first place, we felt that—

Senator FLETCHER (presiding). At any rate, you did not subscribe?

Mr. McQUAID. No. We had our troubles down there two years before, and we had not had the country come to our help particularly.

Senator GLASS. We thought in this provision that we were giving member banks an opportunity to secure additional profits out of their investments in the Federal reserve system. We thought this would be one of the most attractive things that we had in the bill. It is so attractive that many people want us to take it out altogether and pass it anyhow.

Mr. McQUAID. Senator, if it were not for the reserves that we carry with the Federal reserve bank, the Federal reserve bank would not pay dividends, could not pay expenses.

Senator GLASS. Then, would you not be willing to concede that if it were not for the Federal reserve system, that insurance against a currency panic, many banks in this country would be in a frightful situation?

Mr. McQUAID. I am heartily in favor of it and putting in that part of my insurance.

Senator GLASS. Do you think that without the Federal reserve system we could have survived the shock of the World War?

Mr. McQUAID. I agree with you.

Senator GLASS. Do you think that without the Federal reserve system we could have survived the shock of 1928 and 1929 on Wall Street?

Mr. McQUAID. We had to have something of that kind.

Senator GLASS. Is not insurance worth anything to a member bank?

Mr. McQUAID. This corporation is not an insurance corporation, Senator; this is a liquidation corporation, Senator.

Senator GLASS. I know, but we think it will make money, and if it does, 30 per cent of its profits will go to the member banks.

Mr. McQUAID. I would rather forego my chance of getting profits.

Senator GLASS. Well, of course that is a question of judgment.

Mr. McQUAID. I say that the Federal reserve system in its capital would not make any money.

Senator GLASS. Neither could the capital of your bank make any money.

Mr. McQUAID. How is that?

Senator GLASS. I say, neither could the capital of your bank make any money. You make the money on your deposits.

Mr. McQUAID. No; that is right.

Senator GLASS. Although one witness made the amazing statement to me and to the committee that he made more money out of capital of his bank than he made out of the hundreds of millions of deposits. I do not know exactly how he managed it.

Senator WALCOTT. Would you rather have this provision temporarily existing during a period of crisis, for instance, or extreme deflation or depression, or would you rather have it permanent? If you are going to have it at all and if you got it so that it would suit you in its provisions, would you rather have it a temporary, emergency thing, or would you rather have it permanent?

Mr. McQUAID. Are you speaking of the bill as a whole?

Senator WALCOTT. No; I am speaking of this liquidation corporation that we are now discussing.

Mr. McQUAID. Oh, I think this liquidation corporation is intended to be a permanent corporation.

Senator WALCOTT. It is in this bill, but I say, does it help it any in your mind if it should be transformed into an emergency measure?

Mr. McQUAID. I think that makes little difference.

Senator WALCOTT. Makes little difference?

Mr. McQUAID. If they are going to form a liquidation corporation, why, it might just as well be permanent as temporary.

Senator GLASS. One part of that provision, though, you know, is temporary, that which relates to nonmember banks.

Mr. McQUAID. Yes.

Affiliates and branch banking: I think there should be stricken out of lines 21 and 22 of section 21:

"If such establishment and operation are at the time permitted to State banks by the law of the State in question."

Senator GLASS. You think we ought to go into the States, whether they want us or not, with national banks?

Mr. McQUAID. Yes, sir.

Holding companies were created because Federal law did not, and many States do not, permit state-wide branch banking.

As a bank having affiliated banks in our State we would welcome the opportunity to convert these separate affiliated banks into branches and feel that other banks having affiliated banks would do likewise. There would not be any need for any regulation of any holding corporation so far as we are concerned if you are able to do that.

Senator GLASS. You know, one witness only to-day protested against the invasion of State's rights to the extent of 50 miles across the border from the bank.

Mr. McQUAID. My preference, Senator, would be to confine it to State limits.

Senator GLASS. Whether the State law permits or not?

Mr. McQUAID. Whether they permit it or not. Why should the Federal law, enacted to give a national, uniform system of banking, be modified and hampered by laws of any one of 48 States, or the national banks of 1 State denied the facilities or rights given national banks in another State?

Senator GLASS. I am not disagreeing with you if you could get an assurance that you could get the branch banking through Congress. I do not think this committee would largely disagree with you.

Mr. McQUAID. That would eliminate to a very considerable extent some of these difficulties about holding corporations.

Senator GLASS. I would like you to have the job of managing a bill like that through Congress. It took us 16 months to get the small measure of branch banking in cities and counties.

Mr. McQUAID. The provision in section 2, paragraph 2, that any corporation, regardless of whether it is a corporation whose principal purpose is holding bank stocks or is a corporation handling investment securities, is termed an affiliate if the shareholders owning a majority of the bank's shares control the corporation or if a majority of the directing officers of the corporation are directors of the bank, is entirely too drastic, as is also the provision in section 18 that no director, officer, or employee of a member bank shall engage or be an officer of a corporation which engages in the business of making loans on collateral regardless of whether they are primarily dealing in investment securities. This will disqualify directors who are in no way connected with the investment banking business.

I mentioned the naval stores business. We have a director who is president of one of the large naval stores corporations. They make advances to the naval stores operators. Under the terms of this bill

that director would have to resign. We would lose two other directors for similar reasons, because their companies loan money on collateral. We have always thought that it was very desirable that a director represent the different business interests in that community, get the benefits of the advice of people in different lines of business. I think still that is desirable, and I hate to see anything of that kind curtailed, which this will do.

Senator GLASS. You were opposed to the Clayton Act, were you?

Mr. McQUAID. Sir?

Senator GLASS. Were you opposed to the Clayton Act, that provision of it relating to interlocking directorates?

Mr. McQUAID. It did not bother me much. I did not pay much attention to it. We have gotten permission from the comptroller's office under the Clayton Act to have officers of our bank act as officers of our affiliate banks. We are not bothered very much about that. Incidentally, we have another corporation that this would apply to. I suppose we would have to liquidate the corporation. It is organized for the purpose of handling real estate mortgage loans, because we do not believe in the bank making such loans; but under the terms of this bill we would have to close it up, I expect, and get out of that business. I do not know whether it is necessary for us to go that far or not, but they are supplying a need to the community there that it seems to me is very necessary. But I say, I think generally under the terms of this bill it looks to me as though that would be the result so far as we are concerned. It is broad enough to cover that.

Further, the bank is prohibited from receiving deposits from such corporations, firms, or individuals loaning money on collateral. Such drastic provisions are entirely unnecessary and will prohibit the bank from doing business with many depositors who are in no way connected with dealings in investment securities.

Is the investment banking business so discreditable that banks must disassociate themselves from those engaged in it in every way? While in the opinion of some it may be desirable that banks no longer engage in the distribution of investment securities, the investment banking business is lawful and an honorable business. Those associated in it are desirable as directors of a bank and as customers and depositors.

Under the provisions of section 19 no corporation or partnership owning more than 10 per cent of the capital stock of a bank is permitted to vote the stock unless a permit is received from the Comptroller of the Currency, even though the ownership by the corporation or partnership is incidental to their real business, and such permit will not be given if they engage in the distribution of securities, and unless, among other things, reports be given periodically to the comptroller and permission be given to an examination by national bank examiners.

While it may be desirable to require reports and permit examination of affiliate holding companies of banks owning control of affiliate banks—I have no objection at all to that—these restrictions in other corporations owning more than 10 per cent of a bank's stock are unnecessarily severe, at the most they should only be required to satisfy the Comptroller of the Currency that they had

sufficient other assets to meet any stock assessment that might be levied upon bank stocks held.

I am perfectly in accord with the idea of regulating the affiliate holding company such as ours is. We have a corporation whose stock is indorsed upon the stock of our bank. It holds only bank stocks, banks that we are interested in. I am perfectly willing that that corporation be examined as many times as the comptroller wants to examine it, and I am willing to comply with all the regulations you have provided in there, because that is strictly a holding company of bank stocks. I am perfectly willing to create other assets that are sufficient to cover the par value of bank stocks. As a matter of fact, we have cash now for almost the par value of the bank stocks held in that corporation.

But when it comes to other corporations where they own bank stock and their ownership is incidental, I think that is pretty severe. Other lines of business are not going to permit examination by Federal examiners.

Some of the radical changes and restrictions proposed in the present bill, to which only brief reference can be made here, can work tremendous harm to the banking and business interests of our country. Changes should be made only after careful consideration, both from the standpoint of actual practice and experience as well as theory.

Senator GLASS. What would you call careful consideration, sir? We have been working on this bill since February of last year.

Mr. McQUAID. Well, Senator, the first thing I knew about this bill was about a month ago.

Senator GLASS. The fundamental features of it were contained in a bill that I introduced in the Senate on the 7th of June, 1930.

Mr. McQUAID. I doubt if there are very many banks in this country that have analyzed this bill.

Senator GLASS. So do I, sir. And do not mistake my smile when I say that. Therefore, I wonder that they should have been induced to wire their respective Senators very definitely against the bill, if they have not understood and seen it.

Mr. McQUAID. I think instead of wiring they would have been here had they read the bill. That is the reason I came.

Senator GLASS. They are here, are they not?

Mr. McQUAID. Understand, I am heartily in accord with constructive legislation, but I do not like to see something done that is going to hamper the operation of a bank in a local community, that is going to make the Federal reserve system less attractive to the banks, because I think one of the things that you ought to try to do is to make it more attractive and get more banks into it.

Senator GLASS. Well, so do we.

Mr. McQUAID. Part of our troubles is very largely because there are 48 system outside of the Federal reserve system, different kinds of regulation. The failure of those smaller banks surrounding the national banks have had the effect upon all of us.

Senator GLASS. If you can devise a provision of this bill or devise a bill that will enable the constitution of it to create a uniform system of deposit banking, we will be obliged to you. We find that the Attorney General of the United States can not do it.

Mr. McQUAID. Do you think, Senator, that the Congress can not pass a provision in there that you can provide for state-wide banking irrespective of State laws?

Senator GLASS. Oh, that has been determined by the courts; yes, we can do that. But I am talking about a uniform system of banking.

Mr. McQUAID. Well, I think the other will come.

Senator GLASS. Maybe so.

Mr. McQUAID. By a process of elimination.

Senator GLASS. We have not ingenuity enough to devise a provision that would be considered constitutional.

Mr. McQUAID. Make it attractive to the banks that do come into the system.

Senator GLASS. I mean it would make it so attractive that there would not be any State banks left, provided we let them in the system, if we could do that.

Mr. McQUAID. The small, independent State bank is going to have a hard time, then.

Senator FLETCHER (presiding). Mr. McQuaid, how many affiliates has the Barnett Bank?

Mr. McQUAID. Four banks.

Senator FLETCHER. And how many has the Florida National at Jacksonville?

Mr. McQUAID. Outside of Jacksonville they have, I think, six.

Senator FLETCHER. And how many has the Atlantic Bank?

Mr. McQUAID. They have five outside of Jacksonville. I am not counting the suburban banks.

Senator GLASS. That would mean that they would all become branches under the state-wide banking system, would they not?

Mr. McQUAID. I am only speaking for myself, but I am satisfied the other two would. And then there is Mr. Romph's bank, the First National Bank of Miami, that has affiliated banks, and they, I think, would all welcome the opportunity of assimilating those banks with the parent bank and operating as branches.

Senator FLETCHER (presiding). Any other questions of Mr. McQuaid? That is all, then, Mr. McQuaid. We are much obliged to you.

Mr. Edward W. Lane, who is chairman of the board of the Atlantic National Bank of Jacksonville, has been unable to come, and he writes this note (reading):

The bearer, Mr. Edward Ball, of du Pont-Ball Co., who is the controlling spirit in the Florida National Bank of Jacksonville, has been requested by me to represent the Atlantic National Bank of Jacksonville, and its affiliated banks in the Atlantic group, in opposing the objectionable features of the Glass bill, particularly the group banking provision.

We trust the committee will recognize his representation of us.

Very truly yours,

E. W. LANE,
Chairman of the Board.

STATEMENT OF EDWARD BALL, REPRESENTING DU PONT-BALL CO. AND ATLANTIC NATIONAL BANK, JACKSONVILLE, FLA.

Senator FLETCHER (presiding). So Mr. Ball, will you speak now for Mr. Lane and tell us your views about this bill?

Mr. BALL. Mr. Chairman, I am not a technical banker. I trust that the members of the committee will bear with me when I do not follow them on technical points.

The Florida National group, which I represent—and Mr. Lane has asked me to represent the Atlantic National Bank—is also opposed to the provision that the company owning more than 10 per cent of the stock is to be subject to examination by the Comptroller of the Currency's examiners. Our bank stock is only incidental in our business, though we operate seven banks in the State of Florida. It is a very small percentage of the business of the corporation, and we certainly do not expect to have the comptroller's office examining the books of our corporation four times a year.

Senator FLETCHER. What is your corporation?

Mr. BALL. The Almour's Securities (Inc.). We are certainly opposed to the provision in this bill that will require the member banks to subscribe a certain per cent of their capital to a liquidating corporation. We believe that when we are operating a line of business, we should try to make a profit, not to absorb the losses of some people who are not fortunate enough to be able to operate on a profitable basis.

Senator BULKLEY. You understand that that is intended to absorb losses?

Mr. BALL. It is my belief that that is exactly what it will have to do.

Senator BULKLEY. Why so?

Mr. BALL. If a bank had such poor receivables that it closes up, how can anyone make money out of liquidating some of those receivables?

Senator BULKLEY. Does it not depend on what it gets out of them when it liquidates them?

Mr. BALL. Perhaps so, Senator.

Senator BULKLEY. Why perhaps? Does it not depend on that?

Mr. BALL. Yes, sir; and the comptroller's office apparently insists on getting your last dime for the depositors of the closed bank, and he does not seem to be interested in the success of the bank who buys those.

Senator BULKLEY. The liquidation corporation is not obliged to buy at anybody else's price?

Mr. BALL. That is true, Senator. We have had to purchase some assets of closed banks in our own experience to be able to get a charter.

Senator BULKLEY. That is different from the liquidating corporation. It does not have to buy any assets of closed banks.

Mr. BALL. Senator, would you suggest even that the liquidating corporation is going to sell assets for less than their value? Would that be fair to the depositors of the closed bank?

Senator BULKLEY. I suggest that they are not going to buy them for any more than their value from the closed bank.

Mr. BALL. If they pay them their full value, how can they make a profit, Senator?

Senator BULKLEY. If they pay them their fair value they have the profit of closing them out, of course. Of course, in buying they allow for the probable expense of selling them, and they buy at a price that they presume they can make money on; and they are pre-

sumed to buy at so much less than a price that they can make money at that it is actually provided that they have to give back any excess over and above a reasonable fee for closing out. Certainly it is not contemplated that they are going to buy them for any exorbitant price or even their fair price. The whole contemplation of the act is that they shall buy them for less than they can sell them for, and for substantially less than they can sell them for.

Mr. BALL. Would not the receiver of that bank be guilty of defrauding the depositors in the defunct bank if he sold them for less than they were worth?

Senator BULKLEY. Why, certainly not, because any excess that is realized from their liquidation comes back to them.

Mr. BALL. Comes back to the receiver?

Senator BULKLEY. Yes.

Mr. BALL. Then, Senator, how can the liquidating corporation make any profit other than its liquidating expenses?

Senator BULKLEY. It makes the 6 per cent.

Mr. BALL. If a bank can only make 6 per cent on its capital, Senator, do you think it could continue in business long?

Senator BULKLEY. That is not what it is figured on; 6 per cent of the amount realized. Have you read it at all?

Mr. BALL. Yes, sir.

Senator BULKLEY. Isn't that what is in it?

Mr. BALL. I read it in the press.

Senator BULKLEY. It hasn't anything to do with 6 per cent of the capital, has it? It is 6 per cent of the amount realized?

Mr. BALL. Six per cent of the amount realized.

Senator BULKLEY. Then why are you talking about the 6 per cent on the capital?

Mr. BALL. I gather, Senator, that you could only make 6 per cent on your capital.

Senator BULKLEY. Not at all. There is no limit.

Mr. BALL. I thought it might be like the interstate commerce.

Senator BULKLEY. Not at all. We expect the liquidating corporation to make much more than 6 per cent on its capital.

Senator BROOKHART. Does not all capital in the United States make less than 4 per cent?

Mr. BALL. Senator, I am convinced of that fact.

Senator BROOKHART. You do not want the banks to have a special privilege of making more than anybody else, do you?

Mr. BALL. At the present time, Senator, I think that most capital makes less than 2 per cent.

Senator BROOKHART. It has made less than nothing since 1928.

Mr. BALL. Yes, sir. It would seem that this bill is an attempt to regulate management into banks. Now, if it is desirable to regulate management into banks, why is it not desirable to regulate management for the grain growers, the cattle growers, the canneries, and every other industry?

Senator GORE. The Farm Board is doing that for the grain and cotton people.

Senator BROOKHART. Now let us talk about that just a minute.

Mr. BALL. But, Senator, they appear not to have been successful for the grower.

Senator BROOKHART. The Farm Board has regulated us into trouble, there is no doubt about that. But take the banks; the cooperative banking systems all over the world have a regulation first fixing the earning of capital, wage of capital, just like you fix wages for men; and second, they have a regulation absolutely prohibiting the use of any credit for speculative purposes at all. It is arbitrary, absolute; there is not any condition or ifs and ands about it. If you are familiar with those you will find that those cooperative systems in any country where they exist are sounder and safer and better to-day than any of your competitive banking systems. So those are very drastic regulations, are they not?

Mr. BALL. Which countries have the cooperative banking systems?

Senator BROOKHART. Well, Great Britain and France has it developed since the war, and Germany, the Raiffeisen and Schulze-Delitzsch, went through the war and through the deflation and came out sound, when everything else blew up until the Government helped it out, and Denmark has a magnificent system. Czechoslovakia has one that is almost perfect, and Bolsheviki Russia has a magnificent system.

Senator GLASS. When did you come to the conclusion, sir, that there should be no regulation of banks and banking management beyond that akin to the regulation of other enterprises?

Mr. BALL. Senator, I did not assume that banking was essentially different from other enterprises, and I do believe—

Senator GLASS (interposing). You did not?

Mr. BALL. Not necessarily; no. And I do believe that this country was built up on individual initiative and individual management of business and not in regulation from Washington.

Senator BROOKHART. Now let us talk about that a minute. Take a corporation. Does the individual vote at all in any corporation in this individual country of ours? It is not the capital, the stock that votes, and not the individual?

Mr. BALL. That is true, Senator.

Senator BROOKHART. Where is your individuality, then, under a system that wipes out all individuality?

Mr. BALL. There is an individual management there.

Senator BROOKHART. Under your cooperative system one man has one vote, regardless of how much stock he has, and those are sound systems in the world, even in this world of depression. But your so-called individuality is a misnomer in the United States.

Mr. BALL. Senator, I believe you are going back to—was it not Daniel Webster's question as to whether the mule or man voted, he had to have at least a mule before he could vote?

Senator BROOKHART. They used to have such a rule as that in his days.

Senator GLASS. It looks to me as if you are going back to the primitive system before the organization of banks when you say that institutions that control all of the credits and practically all of the deposits, that issue all of the currency with which we transact business, ought not to have any supervision or regulation.

Mr. BALL. Senator, do they not have a regulation to-day, and supervision?

Senator GLASS. Yes; but you are not in favor of it.

Mr. BALL. I had not advocated intentionally—if I had advocated doing away with the regulation and supervision that they have to-day, it was unintentional.

Senator GORE. How did they decide? Who did they decide voted, the man or the mule?

Mr. BALL. I have forgotten which.

Senator FLETCHER (presiding). That would depend on who had charge of the election. In some precincts where Peter Jones came up on a mule, when they asked Peter Jones how he wanted to vote, he says, "I am voting the Republican ticket." "How did you come, Peter?" "I came on a mule." "Well, put Peter Jones down voting the Republican ticket and Mr. A. Mule voting the Democratic ticket." [Laughter.]

Go ahead, Mr. Ball.

Mr. BALL. If it is desirable to have banks subscribing to a liquidating corporation to close out the defunct banks, why would it not be equally as desirable to have all corporations which own newspapers subscribe a pro rata amount of their capital to liquidate the failed newspapers and make such profit as there were in liquidating them or absorb such losses as there might be—or any other line of business?

Senator FLETCHER. Do you recognize the banking business as a quasi-public business, Mr. Ball?

Mr. BALL. Yes, sir; Senator. Are not most businesses quasi-public?

Before we had quite so much regulation it appears that the banks did not fail as frequently as they have failed since we have had some of this regulation.

Senator GLASS. I am not smiling at that; I am laughing outright.

Mr. BALL. That is what I thought, Senator, and I have here a newspaper clipping from a newspaper for the 10 years, 1911 to 1920, both inclusive, showing that there were 762 banks failed in the United States. For the 10 years, from 1921 to 1930, inclusive, there were 6,477 banks that failed in the United States.

Senator GLASS. All due to regulation, was it?

Mr. BALL. I would not suggest, Senator; I would not presume to suggest what caused the increased failures.

Senator BROOKHART. There was too much of this individuality that you were talking about.

Mr. BALL. Senator, I believe individuality has been repressed considerably since 1920 in banking, as in other activities in the United States.

Senator BROOKHART. Been repressed more and more, ever since the first corporation was ever organized, the British East India Co. That is the first one, I believe.

Mr. BALL. Well, Senator, I am not familiar with how much individuality there was at the time of the British East India Co., but it certainly seems that there is less room for individuality each year under our increase in the number of bureaus in the United States, and it is a fact that the cost of government per capita in the United States has been increasing tremendously in the last few years.

Senator BROOKHART. Yes; I heard about that. I also heard that Mr. Grace of the Bethlehem Steel Co. drew down a \$12,000 salary and \$1,625,000 bonus, which is more than all the salaries of all the

Senators in the United States, and their secretaries included. I am in favor of reducing those salaries.

Senator GLASS. If you would let Mr. Grace answer, he would say he is worth more than all the Senators of the United States.

Senator FLETCHER. Is there any other point in the bill you want to allude to, Mr. Ball, any further provision?

Mr. BALL. Senator, there is one point in the bill on branch banking that we do favor. We believe branch banking would be a good thing, either within the State or throughout the United States. The Senator here spoke just a moment ago of the British system, which is a branch-banking system.

Senator BROOKHART. I was not talking about the branch-banking system; I was talking about the cooperative system. I am opposed to branch banking.

Mr. BALL. Senator, I thought in the British Isles they had branch banking.

Senator BROOKHART. You know they had a cooperative system with \$1,000,000,000 in it, cooperative, not any of your competitive system, where they let one man vote regardless of how much stock he owns and where the earnings of the capital were absolutely fixed and where the use of credit for speculation is absolutely prohibited. You did not know about that system at all?

Mr. BALL. Senator, don't we have a competitive system in the Dominion of Canada which is strictly a branch-banking system, and where they have had so few bank failures since that system was installed?

Senator BROOKHART. We just checked that over. They had 11 banks. Of course, they have many more branches, and they have had 16 failures; so it was about 140 per cent in failures in Canada in their system since it started. So I do not know as they are any better off on that than your individuality.

Senator FLETCHER. Is there anything more, Mr. Ball?

Mr. BALL. There is only one thing, Senator. I was just going to remark to Senator Brookhart that under the individual system of banking in Florida we have to-day, I was told by one of the members of the Comptroller of the Currency's staff, that the banks in the State of Florida were the most liquid banks in the United States, banks that are in stronger position financially than in any other State.

Senator BROOKHART. I noticed a long list of them that failed down there a little while back.

Mr. BALL. That is true.

Senator BROOKHART. And I noticed somebody trying to get there with some money in an airplane to save them and did not get there in time.

Mr. BALL. There were a lot of them that failed, but I do not think there were nearly as many of them that failed in Florida in the last year, possibly, as they did in Iowa. Ours failed before yours did.

Senator BROOKHART. There was 55 years that we did not have many failures in Iowa to amount to anything.

Mr. BALL. We hope not to have any failures in Florida in the next 55 years.

Senator BROOKHART. Then, whenever you get too much of this individuality you will have plenty of them.

STATEMENT OF SPENCER S. MARSH, VICE PRESIDENT AND CASHIER NATIONAL NEWARK & ESSEX BANKING CO., NEWARK, N. J.

Mr. MARSH. I am here at the request of the New Jersey Bankers Association. While I have no written thesis I want to present to your committee, sir, if I can, what we think in New Jersey this bill will do to banks of our class, banks that run from fifty to one hundred million dollars worth of assets, that have been serving an industrial and manufacturing community, that have not been actively practicing investment banking or interested in stock-market problems except as they have been using their funds in purchasing high-grade bonds as a secondary reserve. While I have been listening to the various gentlemen who have appeared before you, I find that a number of them have taken some of my thunder, and I hesitate to bring up subjects that have been discussed by them.

Senator FLETCHER. Are your banks nonmember banks?

Mr. MARSH. No, sir. Ours is a national bank. There are both in New Jersey. There are a great number of them.

Senator FLETCHER. You are speaking for the national banks or the member banks?

Mr. MARSH. I am speaking for the New Jersey Banking Association, which has both members. Our bank is a national bank and has been ever since national banks existed. We are 128 years old.

My first memorandum is that as a class our various institutions that I have been in communication with do not like to have to contribute to your liquidating corporation stock. In our own instance it means that we have to contribute \$350,000 for that purpose, and we feel that it is too large an amount for medium-sized banks to contribute as an insurance fund, if we could use that term. Some of you Senators did use that term, I think, while we were talking.

Senator GLASS. What is the total volume of your deposits?

Mr. MARSH. \$35,000,000. Total assets of \$41,000,000.

Senator FLETCHER. Do you have any affiliates?

Mr. MARSH. Well, we have a securities corporation that is an affiliate, that is only used as an affiliate to buy customers' stocks or investments, bonds, and investments which they want. They do not go in it as a business. We have a real estate affiliate that owns the building we are in, so we are not disturbed about those features of the bill. We would rather use our \$350,000 in the banking business, and would rather have this liquidating corporation divested from the Federal reserve act.

One of the features in your bill that disturbs us as much as anything or more than anything is the restrictions on the 15-day loan. That has come to be a very useful means for financing institutions such as we are. There are a large group of them in the State—institutions that are practically all commercial banks with small amounts of savings deposits whose depositors carry large amounts, and they fluctuate. It means that it is easier for us to take Government securities to our Federal reserve bank and use that method of borrowing, rather than commercial paper. Commercial paper has disappeared, so far as we are concerned, in a very large measure, and it has disappeared because a large number of our customers

who were corporations, during the easy money of 1928 and 1929 financed their needs by issuing stocks and bonds, and got out of the necessity for issuing commercial paper with which to finance themselves. In our particular case, our commercial paper has shrunk from a volume of \$20,000,000 down to \$10,000,000. Our commercial paper before that time ran in large pieces, and was used by manufacturers to finance themselves. The ease with which they sold their securities took them right out of that market, and now it is much easier for us. We have about 8 to 10 billion dollars' worth of commercial paper.

Senator BROOKHART. Is not that enough for your rediscount demands?

Mr. MARSH. Yes; plenty; but it is much easier for us and easier for the Federal reserve bank to send them some Government securities and borrow on that. The reason for it is—one of the Senators, I believe, asked that question—the reason for it is that there are times when the large accounts drop quickly and we are short a temporary time, until we get our money and pay it off again, in the next 30 days, probably.

Senator FLETCHER. These corporations issue stocks and bonds and relieve themselves in that way, unloading those on the public?

Mr. MARSH. Yes; in a good many cases.

Senator FLETCHER. And most of them have depreciated?

Mr. MARSH. Oh, yes. They helped supply a large amount of the stocks that depreciated.

Senator BROOKHART. Have the banks unloaded on the public?

Mr. MARSH. No, sir. Some of them may have, but I do not know of any bank that did.

Senator FLETCHER. Your bank does not engage in distribution of securities?

Mr. MARSH. No, sir; not at all.

Senator BROOKHART. It was the bank affiliates that did that?

Mr. MARSH. I know of no bank in Newark that did it, and I do not know any in New Jersey that did it. Although New Jersey is right under the influence of the metropolitan practices, they have never distributed that class of securities as banks. The objection we have to that, Mr. Chairman, is that by putting the rate 1 per cent higher than the rediscount rate, it puts a penalty on that operation and prevents us from making loans, as one of the witnesses said; and I would like you gentlemen to get this picture. We are a sort of self-contained community with a good many securities and a large number of comparatively small people who have securities that they come to the bank and borrow on. We have about \$6,000,000 worth of demand loans that are made up of loans on collateral, and, I think, it is not touched by anything that is in your bill; but if we wanted to make some of those loans while we were borrowing we could not do it.

Senator TOWNSEND. What is the collateral?

Mr. MARSH. Some of it is stock-exchange collateral. Some of it is local stocks, and some bonds.

Senator TOWNSEND. Why would it not be covered in this bill?

Mr. MARSH. Because you say in there, in the bill, that while we are borrowing on a 15-day loan we can not make collateral loans. That goes back to your definition of "collateral," I suppose.

Senator GLASS. But we do not exactly say that.

Senator TOWNSEND. No.

Senator GLASS. We say that when your bank is put upon notice by the Federal reserve bank that you are already too far extended in stock-exchange loans you can not make use of the facilities of the Federal reserve bank if you persist in still further extending the loans.

Mr. MARSH. As I read it, Senator, I read it as prohibiting that class of loans. If that is true, I would like to know it.

Senator GLASS. No.

Mr. MARSH. My other objection is, I think that class of borrowing which definitely serves a definite purpose and, I think, a legitimate purpose should not be penalized with the 1 per cent higher rate.

Senator GLASS. That may be. That is a matter for further consideration, although it has had very serious consideration. Suppose that should be abated or eliminated, although you understand the Federal reserve bank now has the unrestricted right to make that percentage whatever it may please.

Mr. MARSH. Yes.

Senator GLASS. And you are assuming because it has not done it it never will do it, and I think your assumption is correct, I am sorry to say.

Mr. MARSH. I hope it will.

Senator GLASS. With that eliminated, what objection would you have to that provision?

Mr. MARSH. I do not think I would have any.

Senator GLASS. Very well.

Mr. MARSH. The increase of reserves is my next topic. There is another item I want to take up before that, if I may, and that is the question of real-estate loans. The bill provides that we can make a total of 50 per cent of our time deposits; that in figuring the total of loans it must take in all of those loans that depend for their final base on real estate. In New Jersey we have, unfortunately, a building-loan situation. The banks of New Jersey are loaning building loans at the present time, some \$63,000,000, and we are trying to adjust things so that we can all go along as we should. If it is necessary to figure the total of those loans in our real-estate loans it is going to throw us way above the 50 per cent and will work a very clear hardship on the building loans, and they are in bad enough situation right now.

The CHAIRMAN. They are getting relief under this Reconstruction Finance Corporation?

Mr. MARSH. Yes; some of them are getting it. That has helped conditions very materially. Both the Reconstruction Corporation and the Glass-Steagall bill are helping the conditions there very materially. But this real-estate feature would work a very real hardship at the moment because of the inability to get rid of our mortgages. There is no mortgage market under the conditions that exist to-day, and there is no real-estate market. That is one of the reasons and back of the reason why we feel that the bill should not be passed at this time.

Senator GLASS. You know that relates to loans hereafter? You observed that?

Mr. MARSH. Not to those that we have?

Senator GLASS. No.

Mr. MARSH. I read it as though it referred to the present time.

Senator GLASS. No; I suggest you read it over again.

Mr. MARSH. I will.

The segregation of the time deposits: A large number of the banks in New Jersey have small amounts of time deposits. Some of them have a larger percentage of time deposits than they have demand deposits. We feel that it would discriminate against our demand deposits and would promote the withdrawal of those demand deposits.

The question of reserves, which I have here, would work a hardship on banks that are at the present time struggling to make profits. New Jersey suffered, I think as some of the rest of the country did, by an overproduction of banks, both national and State banks, and at the present time they are trying to have that adjusted. A good many of the banks are not making any money. If you put a burden of this kind on, although it is graduated and does not all become operative, we feel that it is going to be a little heavy—too heavy for the banks to make proper profits, because, after all, banking, as everything else, must make money or it can not exist.

Senator GLASS. How do you figure, sir, that one-fourth of 1 per cent on \$35,000,000 of deposits would require you to pay \$350,000?

Mr. MARSH. One-fourth of 1 per cent?

Senator GLASS. Yes.

Mr. MARSH. I thought it was 1 per cent.

Senator GLASS. No.

Senator TOWNSEND. \$87,500, I think.

Senator GLASS. Yes.

Mr. MARSH. I figured 1 per cent, \$350,000. That is what I figured on. Whatever it is, we do not want to invest it. We would rather have our—

Senator GLASS. Of course, not. You would like to have all the profit of the operation.

Mr. MARSH. No; we are willing to give the other fellow a break, but what we want to do is to invest it in our banking business.

Senator BROOKHART. Would it not help your banking business to open its closed banks?

Mr. MARSH. Our experience in New Jersey has been that almost in every case where a bank is closed there has been bad banking behind it. There may be somewhere that has not been so; but it has not been only the one thing; it is a combination of a couple of things: Bad banking somewhere in the past and the present crisis has brought it to a head. I may be wrong but I think it would be a very healthy thing for some of those banks not to be opened.

Senator BROOKHART. You do not think these 8,000 banks have failed in the United States because of bad banking, do you?

Mr. MARSH. No. I have not enough knowledge of those, really, Senator, to have a definite opinion, but I have enough knowledge of the New Jersey situation to know what happened in a good many of those cases: Not all bad banking—I do not say that—but I said in a great many instances it was predicated on bad banking and the present situation brought it to a head.

Senator GLASS. Did not bad banking bring about the present situation?

Mr. MARSH. Yes. I think it did.

Senator BROOKHART. In big places and big banks that reached out over the whole country?

Mr. MARSH. Yes; I think it did.

Senator BROOKHART. And they ruined our little banks and bankers.

Mr. MARSH. My feeling, Senator, is that there was an overproduction of banks, both national and State banks, all over the country.

Senator BROOKHART. I think there was an overproduction of speculation.

Mr. MARSH. I agree with you there, too. It seems to me that the bill in aiming to curtail the practices of large metropolitan banks, particularly in security centers, penalizing banks such as I have tried to describe, which are honestly trying to meet their responsibilities in industrial communities. I am not trying to paint an ideal situation, and I do not believe that all bankers such as I described are without some fault, but I do feel that in trying to reach this control of affiliates, there are penalties and restrictions in the bill that will react on banks, such as I have described, and make it harder for us to operate.

Senator GLASS. What happened, sir, was that some of the experienced bankers who testified before the committee and upon whose testimony the bill was drafted, were divided in their expressions of judgment between the abolition of affiliates altogether, their separation from commercial banks, and more or less severe oversight of them. We tried to strike a happy medium and did not abolish them but proposed to regulate them.

Mr. MARSH. Well, we have no objection to the regulation of affiliates. That, I submit, is justified. We do not object to that.

Senator GLASS. You, neither in your New Jersey banks, nor in any other banks for that matter, are penalized along with banks in many centers unless they follow the vicious practices which those banks followed in making excessive and alarmingly dangerous loans upon collateral security.

Mr. MARSH. We are penalized if we can not go into this 15-day practice as we have been. We think we are, at any rate.

Senator GLASS. On the 1 per cent proposition?

Mr. MARSH. Yes.

Senator GLASS. That is a special privilege, though.

Mr. MARSH. Well, it has got to be a necessity as well as a special privilege.

Senator GLASS. It has come to be far beyond the intent of the people who put it in the law.

Mr. MARSH. Of course, the intent, Senator, was to take over commercial paper. Now, take our own case, and I think it is only indicative of a great many others. The commercial paper would mean that to cover a loan of \$1,000,000—which is what we get usually sometimes once a month, or twice a month—it would mean we would have to take over 200 or 250 pieces of paper when we have the Government bonds right in our portfolio. It would be

a nuisance to the Federal reserve bank and a nuisance to us. So it is following the line of least resistance.

Senator GLASS. I grant you that it is a medium of facility. In other words it makes more convenient and more expeditious legitimate transactions, and if it were used only for that purpose nobody would ever raise any particular objection except that to the extent that it is used it carries you back to a bond secured currency that you gentlemen for 50 years sought to escape from; but you can very readily see that it was not intended for that purpose, because at the time it was embodied in the act, two years and a half after the system had been in effect, there were less than \$100,000,000 of United States securities that might be used for that purpose, whereas 10 banks in New York over a limited period borrowed nearly a billion dollars.

Mr. MARSH. Yes.

Senator GLASS. Under that provision of the bill.

Mr. MARSH. To use in the market?

Senator GLASS. Yes.

Mr. MARSH. One of the features of the bill—and I would like to know whether I am right in feeling this would touch it—is a situation that exists in some of these small towns. An individual is a dealer in investment securities, distributing mostly municipal loans. Now, I read the bill to say we could not go on and loan that individual money while we were borrowing on this 15-day note. That is a distinct hardship.

Senator GLASS. Oh, no; it does not exclude you at all unless you are borrowing excessively on speculation and have had warning.

Mr. MARSH. One of my friends has just asked me to speak of telephone loans; that is, loans from the Federal reserve bank. We do that right along. We have our securities with the Federal reserve bank and telephone in and get a loan, and send the note in. I do not see that that stops that practice at all.

Senator GLASS. No; but if a telephone is run on the dial system I hope it may stop it. [Laughter.]

Mr. MARSH. I have covered the main features on my memorandum, Mr. Chairman.

Senator GLASS. We are very much obliged to you.

The CHAIRMAN. We thank you.

STATEMENT OF CHARLES F. ZIMMERMAN, PRESIDENT OF THE FIRST NATIONAL BANK OF HUNTINGDON, PA., AND PRESIDENT OF THE STATE BANKERS' ASSOCIATION OF PENNSYLVANIA

The CHAIRMAN. Will you state your name, residence, and occupation?

Mr. ZIMMERMAN. Charles F. Zimmerman; president of the First National Bank at Huntingdon, Pa. I am also secretary of the Pennsylvania Bankers' Association.

I come before the committee with a good deal of diffidence because of representing an interest that seems rapidly to be vanishing in this country, known as the country banker; and I certainly do not wish to create an inference that I speak with authority or finality. I do feel, however, that it is quite pertinent that the viewpoint of the country banker, which I believe in some considerable degree I represent, might be expressed with regard to the provisions of this bill.

The CHAIRMAN. We will be very happy to hear it, sir.

Mr. ZIMMERMAN. First of all, I should like to say that among the ardent supporters of the Federal reserve system there are none more marked than the country banker. There is a very high regard for the administration of the Federal reserve system, particularly as it comes out of the Federal Reserve Board at Washington, and I am numbered among those who believe that for the good of banking in this country it is entirely right and proper that more authority should be lodged in the Federal Reserve Board than heretofore. I say this because of what little experience I have had in business and in connection with the business of a bank and the granting of credits. A house divided against itself can not stand, whether in the matter of a unit bank or whether in the matter of establishing credit on a broad basis affecting the whole country.

Therefore, I am entirely in sympathy with the provisions of the bill that have to do with centering more authority in the Federal Reserve Board. More than that, I am entirely in sympathy with the provision in the bill that seeks to correct the abuse of short-term credit granted by the Federal reserve system to large banks. That there has been abuse, no one who has been observant would attempt to deny. I believe that it has had a very vital effect upon the difficulties that have developed in this country; and with a plan to coordinate the finer judgment of the bankers of America with the judgment of the Federal Reserve Board in respect to the furtherance of those restrictions, I am sure the entire country would be in sympathy.

I had not particularly wished to take your time to discuss any of these provisions at length. I wish to say, however, that in the bill, as I view it, there are many excellent provisions. The subjects treated upon throughout the hearings to-day, have been largely by way of pointing out objections to provisions in the bill, and I do feel that with respect to certain parts of the bill, there should be a great deal of caution used so far as further deflation of our credit position in this country is concerned. I share fully the sense of anxiety that Colonel Ayers expressed, and I think that due regard should be had for his point of view.

The particular clause which arouses my interest, and I might say, amazement, being a country banker in the State of Pennsylvania, which represents approximately one-tenth of the banking resources of the United States, is the section that has to do with branch banking. In connection with my remarks on that section I should like to say that the bane of our banking system as we have seen it develop during that last six or seven years can be predicated upon the word "promotion." If we had not been given to bank promotion in this country as we had, there would not be so much difficulty in respect to banking, nor would there be so much perplexity facing those who wish to straighten out these difficulties. More than that, the burden of the promotional side of banking, as I have viewed it, has fallen tremendously upon the country banker, so much so that his interests have been assailed on every hand, his position as an economic factor has been belittled; and now it seems that those who have scrambled the eggs of what we have heretofore considered sound banking and sound banking methods, are asking to be defended by new legislation rather than reckoned with in respect to the restoration of those

methods which have been time tested during our entire previous history.

I come here without any prejudice in respect to the specific questions hinging upon the development of a certain branch, group, or chain types of banking. I do come here feeling that it is a mistake that Congress should in any way seek to cater to what I choose to call the go-getter spirit in bank promotion, and that we ought to the best of our ability, right about face in respect to the reestablishment of unit banking so far as that may be done. I have listened to the remarks that have been made before this committee by those who have, on their own initiative and, perhaps, in violation of the more conservative standards in banking, gone ahead and built up these banking structures. I have been impressed with this fact, that they have not been bankers in essence or to the extent which would disallow the injection of other than high banking ideals in our banking system. They now seek to hold the ground gained through the sacrifice of those standards and wish to have it become part and parcel of our thought about Federal legislation. To that extent that we yield, it seems to me, more and more we are going to be led into a maze of difficulty from which we might all seek to be relieved in time to come. I have read the hearings that have been held by the Senate subcommittee in respect to the suggestions to be embodied in the Glass bill, and I could not help but feel that very, very little attention was paid to the viewpoint of those who have ardently sought to preserve the best standards in the conduct of the business of banking.

With regard to this question of State's rights, I am simply astounded to think that Congress would seriously consider the proposal to grant the right for a national bank to cross State lines in so-called trade areas. I am at a loss to know where any substantial demand of that sort should arise so far as the practical administration of banking is concerned and so far as the service of banking to its constituency is concerned, except as it relates itself to the promotional idea in banking. Now, I have not a wide experience. I have a wide acquaintanceship with many bankers, not only throughout the State of Pennsylvania but, I should say, throughout the Nation, and I am at a loss to discover where any economic need exists for the Federal Government to grant any branch banking privilege which contravenes the autonomy of our State banking laws.

Senator GLASS. Mr. Zimmerman, I suppose, of course, you have read the report of the Comptroller of the Currency on that program?

Mr. ZIMMERMAN. I have read all of them.

Senator GLASS. You will have noted there that he does not want to confine us to state-wide branch banking, and he does not want to confine us to Federal reserve zones. He wants us to have branch banking in what he indefinitely defines as trade areas.

Mr. ZIMMERMAN. Senator Glass, I try to be open-minded on these questions, but I am just as far—after all of my reading and investigation, from believing that proper ground has been established by the Comptroller of the Currency in his various arguments or by any other agency interested in that question—as I have ever been.

Senator GLASS. Would you advocate state-wide branch banking by national banks in those States that are permitted to have State banks?

Mr. ZIMMERMAN. I am a believer in the equalization of the rights and prerogatives of national banks with State banking systems no matter what they may be.

Senator GLASS. But you would oppose giving the right to national banks to have branches in States which do not permit branch banking in the State system?

Mr. ZIMMERMAN. Unquestionably.

Senator GLASS. I may say to you, as to your suggested opposition to crossing State lines, if you will read the bill you will note that that may be done only in extraordinary circumstances. The case is cited to the committee of banks located in cities, that there are very few of them in this country that cross State lines, and to banks located so near the border as that their main business may be across the border. So it is not the thought of the committee that that provision of the bill would be very largely availed of. The text of the bill is that it may be done only in extraordinary circumstances.

Mr. ZIMMERMAN. Senator, the provisions in the bill may be harmless enough, but its significance only comes out in respect to what results from its application. I have a very clear idea as to what would happen with respect to Pennsylvania if such a privilege were to be granted. For instance—not that I think it is even remotely thought of by any bank—in Philadelphia there would have to be necessarily some compensating privilege granted to the State institution, otherwise, the natural inclination, if there were at least any rivalry between two of the leading institutions in the city, would be to leave the State system, and go into the national system. But the compensating advantage would probably be along the lines of extending branch banking and weakening the regulation of the State bank. That is where I feel the danger lies.

Now, we are talking in terms in this country of strengthening administrative practices of banks and the supervisory processes as between the State and national systems. The only basis on which they can be properly coordinated is the common basis on which they operate. To whatever extent through Federal law you draw a distinction between that parity, you ruin the highest standards; it seems to me, that those of us who try to think sanely on banking questions, have, namely the coordination more and more of the two types of systems and the eventual bringing about of conditions which will induce every State chartered institution, to become a member of the Federal reserve system.

Senator GLASS. Does Pennsylvania permit branch banking at all?

Mr. ZIMMERMAN. Oh, no; not beyond city limits.

Senator GLASS. Then how could this bill affect you?

Mr. ZIMMERMAN. In respect to a possible extension of the right of a Philadelphia bank to establish a branch in New Jersey.

Senator GLASS. Do you think that is very likely under the terms of this bill? What would be the extraordinary circumstances?

Mr. ZIMMERMAN. I fully grasp the significance of your thought; but, Senator, if the experience of recent years have taught us anything, it is that through concentration of banking capital the weight of influence possessed by large banks inevitably brings concussions

and, perhaps, abuses that never were originally thought of when the law was drafted. And so I think if we have learned anything we must get away from the appearance of evil in respect to the extension of the branch banking privilege.

Senator GLASS. Yes. That has been startlingly illustrated in the 15-day provision of the Federal reserve act.

Mr. ZIMMERMAN. Quite so.

Senator GLASS. I must confess I can not see how under the text of this bill any Philadelphia bank would be permitted to establish a branch in New Jersey.

Mr. ZIMMERMAN. I think the right is certainly conceded if the pressure were sufficiently strong to persuade the Federal Reserve Board that it was an extraordinary case.

The CHAIRMAN. In other words, it could only be done by the Bank of the State of New Jersey that has made you feel the need of such an extension?

Mr. ZIMMERMAN. I have no such thought.

Senator GLASS. Should not it be done?

Mr. ZIMMERMAN. The branch-banking privilege accorded a national bank should be upon a parity with that accorded to the State bank, without a single exception or deviation of any kind.

Senator BROOKHART. I was considerably impressed with what you said about this promotion proposition of banking. Did the comptroller and his examiners examining the national banks in Pennsylvania approve investments in listed bonds on the stock exchange? Did he approve that kind of investment as liquid assets?

Mr. ZIMMERMAN. Oh, yes. I have no thought that in any single institution in Pennsylvania the comptroller would have taken strong exception to the method of conducting the bank except in so far as it might have invested in weak assets. In other words, the finer details of banking, as I think of them, have characterized every banking institution. Now, if you make mistakes—

Senator BROOKHART. He might describe those bonds as secondary reserves and recommend them as strongly as that.

Mr. ZIMMERMAN. Oh, yes; there has been a good deal of that; but I would not attribute to the comptroller's office any supposed management of a local bank through the recommendation of particular types of securities.

Senator BROOKHART. Has not that system of banking made the little country banks sustain these big New York promotions all the time?

Mr. ZIMMERMAN. I have not a great deal of understanding of the effect of that intimately within banks, but my discussion with bankers, unit bankers particularly in Pennsylvania, leads me to believe that many of their securities were bought for the purpose of secondary reserves due to their confidence in the big bank responsible for issuing them.

Senator BROOKHART. In other words, they greatly depreciated those same securities?

Mr. ZIMMERMAN. That is quite true.

Senator BROOKHART. And I find in the West that the banks were everywhere loaded up with those stock-exchange securities and now they are frozen up worse than the farmers' loans were preceding them.

Mr. ZIMMERMAN. That is true.

Senator BROOKHART. Is not that a nation-wide system of watered stocks and bonds that is very detrimental to the banking system?

Mr. ZIMMERMAN. Not only that, but international.

Senator BROOKHART. Yes, I agree with you; internationally; and the comptroller, who used every opportunity he had to put out statements for branch banking, was the same comptroller who loaded up these banks with these securities all over the country, is he not?

Mr. ZIMMERMAN. I shall not admit that he loaded them up, Senator. I do not know anything about his official policies or actions.

Senator BROOKHART. You know, his bank examiners said that was good banking, to buy those securities.

Mr. ZIMMERMAN. I do not think any of them ever said it to me in our bank, but they may have elsewhere. I should like to offer this as a closing thought in respect to branch banking: I feel that the mere mention of state-wide branch banking in that clause is a threat more or less to the future of unit banking. I do not feel that state-wide branch banking has proved its case in America. I believe I could produce—

The CHAIRMAN. And it will take several years to find out?

Mr. ZIMMERMAN. Quite so. And I believe I could produce evidence that would be corroborative of that viewpoint, which I would not care to do; but the mere mention of state-wide branch banking as though it were an ideal for the national bank system, is uncalled for. If that whole clause were amended simply to say in respect to branch banking, as was pronounced in the resolution adopted by the American Bankers' Association, that the autonomy of State banking laws should be upheld, I feel that Congress has answered the question so far as the need for preserving the soundness of branch banking methods in America is concerned. I see no reason to depart from it, Senator.

Senator GLASS. Suppose we were to omit from that provision the authorization with respect to crossing the State line in unusual circumstances. What would be the objection to the provision then?

Mr. ZIMMERMAN. I think there is no inherent objection except the one that I have in my mind as to the inference that state-wide branch banking in itself is a tested system and that national banks are ready to go along in any State that might think it was right.

Senator GLASS. Well, do you not think national banks should be permitted to go along in any State that authorizes State banks to have branches?

Mr. ZIMMERMAN. I do. Now, Senator, you realize, perhaps, very much more than I do, that the mere mention of a type of banking in a bill oftentimes results in the layman getting the wrong idea about the whole thing. I think we need to avoid even the appearance of danger if we can do it satisfactorily by the wording of the clause.

Senator GLASS. I have noticed bankers get perverted ideas as well as laymen.

Mr. ZIMMERMAN. Yes.

The CHAIRMAN. You are an officer in the Pennsylvania Bankers' Association?

Mr. ZIMMERMAN. Yes, sir.

The CHAIRMAN. What position do you hold?

Mr. ZIMMERMAN. Secretary. I should like to say, in line with your suggestion, Senator Glass, that after a little more than 31 years of experience in banking, I sometimes wonder whether I have yet understood anything about it, so that I can forgive a layman if he is unable to get it right.

Senator GLASS. I have been induced, almost, to believe to-day that I have not only not understood anything about it but have not had anything to do with it. [Laughter.]

Mr. ZIMMERMAN. May I say in response to that, Senator, I have followed your work with the Federal reserve system and financial legislation from its very beginning. You speak of the opposition, we will say for the sake of a milder word, of the American Bankers' Association. If you have not learned yet where it happened that the bankers had a change of heart, I will tell you. It was at Richmond after you spoke to them.

Senator GLASS. Well, that is gratifying.

The CHAIRMAN. We have two more witnesses here. I want you to finish. I am just saying this for the members of the committee. We want to hear Governor Platt, and Mr. Ottley, of Atlanta, will be the next witness, and that will conclude our hearing to-day. I do not want to close until you are through.

Mr. ZIMMERMAN. I am quite through. I thank you very much.

The CHAIRMAN. I thank you.

Senator GLASS. I do, sir.

The CHAIRMAN. Governor Platt.

STATEMENT OF EDMUND S. PLATT, NEW YORK CITY, VICE PRESIDENT OF THE MARINE MIDLAND CORPORATION OF BUFFALO, N. Y.

Governor PLATT. I was moved to remark, in answer to Mr. Zimmerman, that I wondered how the city of Philadelphia has managed to survive all these years with a branch or two located in it across State lines. The Camden National Bank of Camden, N. J., has had a branch in Philadelphia for almost 120 years, and Philadelphia is still there. That branch was established in the old days when crops used to be moved from the lower part of New Jersey into Philadelphia and was established about 1813 to help move the crops, and it has been there all these years. It was a State bank originally.

Senator BROOKHART. Do you think the idea was that Philadelphia would like to get even with Camden?

Governor PLATT. As a matter of actual fact, branch banking is not a cormorant and does not grow half as fast as its opponents think it will. Maryland, Virginia, North Carolina, and a number of other States have had state-wide branch banking for years, and no bank in Baltimore has got a branch outside the city except in the immediate locality, if I remember right, Senator Glass.

I believe that the only way to stop bank failures is to allow banks to consolidate. Why should they be restricted from consolidating if they do not happen to be located within the same limits? The national bank act curiously provides that banks may consolidate within county limits, but if you do consolidate them within county limits and they do not happen to be within the same municipal

limits, one of them has to be closed, and I do not see any sense in that at all.

Senator BROOKHART. Out in my country they consolidated, and both of them failed afterwards. [Laughter.]

Governor PLATT. I know when I was on the Federal Reserve Board we agreed to a consolidation of two banks that were 30 miles apart—in South Dakota, I think—and it was said that there was a good road between the two towns, and therefore there was no reason why the other town should have a bank. It would seem to me 20 miles is quite a long way to go. I have talked a good deal about branch banking at various times, and I now want to say a few words about the Federal reserve parts of the bill.

The bill restricts the sale of Federal funds. Several witnesses have spoken about that. I do not know what the objection to Federal funds is. Senator Glass, you said it has been abused. I know about the rather amusing shooting of funds across the country in regard to time. Chicago banks close an hour later than New York banks, and the Denver banks close an hour later than the Chicago banks, and the San Francisco banks another hour later. When the banks in New York have funds left over at the close of the day they have sometimes transferred them to the Western cities when the difference of time leaves the banks still open. It does not do any harm. It tends to spread the lower rates of New York throughout the country to some extent, and while it is a little amusing as an example of sharp pencil work on the part of bank managers, it seems to me it is a good thing. It equalizes reserves to a certain small extent. Of course, the actual volume of Federal funds that are transferred is rather small, but so far as they go these are not harmful, but helpful. There have been cases where Federal funds have been furnished to another town in time of stress that were sufficiently large to be of real service. And it enables, I think, Federal reserve policy to be a little better carried out, because, take a city like Chicago; it naturally should have a Federal reserve rate a little higher than the New York rate.

It is pretty hard to make a Federal reserve rate that is right for the big banks that compete with the New York banks and is right for the country banks, and if you can spread New York funds a little bit, even in small amounts to the large banks in the city, the Federal Reserve Bank of Chicago can fix its rate more fairly with reference to its whole district, I think. So I do not see that there is any reason for regulating or hampering the sale of Federal funds.

Since I have been in New York, I have watched the market for Federal funds every day, through the Marine Midland vice president in charge of the bank's reserve. Last summer, for several months, Federal funds sold for one-eighth of 1 per cent—practically nothing. At that rate, if you sell a million dollars you get only about \$25 profit.

Senator GLASS. It is of so little consequence that I am not acquainted with it.

Governor PLATT. That was, of course, an exceptionally low rate due chiefly to Federal reserve policy. The reserve system was putting funds in the market through purchase of Government securities, making money redundant as there was little business demand. My belief is that the Federal reserve system, generally speaking,

ought to regulate the volume of credit in the country through changing reserve rates and not so much through open-market operations, and not through these little mechanical devices provided in this bill. That is, devices giving the Federal Reserve Board power to fix percentages of collateral loans, and so forth. The result of these devices would be to give the board an opportunity to avoid responsibility in relation to rates, and you can regulate the whole thing, I believe, mostly by means of rates.

Senator GLASS. You were in disagreement with your conferees on the board in 1929 as to that proposition.

Governor PLATT. I was, very strongly.

Senator GLASS. And with me, too, for that matter, although I voted to raise the rates on one occasion.

The CHAIRMAN. You were a member of the Federal Reserve Board how long?

Governor PLATT. I was a member of the Federal Reserve Board a little more than 10 years.

The CHAIRMAN. You are now connected with what is called the Marine Midland Corporation?

Governor PLATT. I am vice president of the Marine Midland Corporation, with an office in New York. But I am not speaking for the Marine Midland Corporation. Mr. Rand will be here to speak for the Marine Midland Corporation.

The CHAIRMAN. We have had two requests from the Marine Midland Bank to hear Mr. Letchworth and Mr. Rand. I am thinking that the committee has so short a time that we can only hear one of them and will have to limit him somewhat if we are going to get through with our hearings in the time agreed upon; but, I am not saying that with any suggestion of curtailing the subject you are on. You go ahead, Governor.

Governor PLATT. I have said all I wanted to say.

Senator BROOKHART. Just a minute about that failure proposition. Out in the agricultural States, if the farmers had received the cost of production for their products, there would not have been any bank failures.

Governor PLATT. Well, the failure of no one industry ought to affect the banks. They ought to be on a broad enough base so that what was lost in one neighborhood or industry would be made in another.

Senator BROOKHART. In other words, although a State is predominantly agricultural, the agricultural industry ought not to be able to make it prosperous?

Governor PLATT. Well, certainly when agriculture goes down, and the price of agricultural products goes down, the farmers are hard enough hit then. Their banks will fail a year or two later and take the rest of their money. That is what happens right along. Agricultural prices declined greatly in 1920 and 1921. The banks began to fail in 1922 and 1923 and took the rest of the farmers' money, and there is no good reason for bank failures.

The CHAIRMAN. I agree with you that the farmers took the expert advice, and those that did not lose their money in the banks, if they bought securities, they are getting smaller dividends on them than if they had deposits in good banks.

Governor PLATT. I do not know about that.

The CHAIRMAN. I will admit it is not very simple mathematics.

Governor PLATT. After all, with any kind of judgment, they have still got their securities, and most of them are paying them something. A good many of them are not. But we know in our best years we have had as many as 40 bank failures during the last 25 or 30 years; and somebody said the other day with that, during our best month in 1929, there were 17 bank failures. I think it is a disgrace to have any.

The CHAIRMAN. I saw a magazine article here that was written on the Canadian banking system. Their records show they only had 16 failures in 62 years.

Governor PLATT. They have not had a bank failure in 10 years, and we had 10,000.

The CHAIRMAN. That is exactly it. In the 62 years they have had more failures than they have had banks. They have 11 banks in their set-up.

Governor PLATT. I think so. If you go back into the Dark Ages 62 years, you can find that a good many things have happened.

The CHAIRMAN. The trouble is, when you have a failure, you can not just call it one with 400 branches.

Governor PLATT. The last bank failure in Canada was in August, 1922. That was the Home Bank of Toronto. It had about 62 branches. You can call that 62 failures. It does not compare with the number we had in one year ourselves.

The CHAIRMAN. I am not contending they have the same number of failures we do. But if the only thing we do with branch banks is to recommend them as safe, there is not much we do. The postal deposit will take care of the safety. I am assuming the bank has a function of doing something besides taking care of the safety of the deposits. That is my attitude, but you and I would not agree on that.

Governor PLATT. I am afraid we would not.

The CHAIRMAN. I am not going into that argument any more.

Governor PLATT. I do not think that we need to have nation-wide branch banking. Until recently there was a very nice little bank in Saskatchewan with 25 branches, all in one Province, Saskatchewan, the Weyburn Security Bank. All of the agricultural territory was hard hit. They did not fail. They are in an agricultural territory, but good management or some additional spread of risk through branches in different communities kept them from failure.

The CHAIRMAN. You know there are banks in agricultural sections of this country that have not failed.

Governor PLATT. Yes. They could have been run so as not to fail.

The CHAIRMAN. But there are a lot of them that have not failed.

Governor PLATT. Yes. There are a good many of them that have not failed. They are the ones, perhaps, that were a little bit hard-boiled or considered hard-boiled among the people that they were serving.

Senator BROOKHART. It was the hard-boiled ones that broke down the farmers' values and finally destroyed his credit, and finally destroyed the banks.

Governor PLATT. I hope we shall some day have a banking system that will not fail.

The CHAIRMAN. Let us get this: You say Canada appropriated money to pay their depositors?

Governor PLATT. That was with relation to the Home Bank failure of 1922. The depositors were paid. I understand an act of Parliament or of one of the Provinces was passed to pay the deposits.

The CHAIRMAN. All I know about it was I was in Canada and saw the newspaper item to the effect that one department of the Canadian Government had voted an appropriation.

Governor PLATT. I have heard that such an appropriation was made, but I think the liquidation worked out so that the deposits were covered and the government funds paid back.

The CHAIRMAN. It was a very unusual thing.

Governor PLATT. Yes. May I add that the Home Bank failure was not due to branch banking in any sense, but to outside investments.

Senator BROOKHART. In the agricultural sections, when the banks made loans to farmers that were not liquid because they could not produce anything in six months or nine months, if they were buying these New York bonds, that would injure agricultural credit and agricultural values, would it not?

Governor PLATT. Not necessarily. The banks in agricultural sections have always sent a lot of money to New York. For instance, in your territory in the fall, when the crops come in, if everything goes right the farmers will pay their notes off in the fall.

Senator BROOKHART. If they can get the price to pay them.

Governor PLATT. I say when everything goes well, when they have good crops and good prices, they will pay their notes off. With that money the banks either buy commercial paper or send funds to New York to lend. They can not lend this temporary surplus at home safely—not at that season. If they do they become tied up in real estate or something. Many of them have tried that, and that is one of the causes of bank failures in that country. The only thing they can safely do is to send the funds to New York or lend that money out at low rates on commercial paper, so that they can get the money back when needed. They generally buy paper in the open market or buy New York bonds.

Senator BROOKHART. If the New York bonds were not liquid, the farmers' loans were not.

Governor PLATT. The farmer would not want to borrow in the winter, and he would have no reason for borrowing at the time when the banks had this money.

Senator BROOKHART. Oh, yes; he does. He buys his cattle and feeds them through the winter on his credit.

Governor PLATT. That is in the cattle-feeding territory; yes.

Senator BROOKHART. That is the territory I mean.

Governor PLATT. There is always a surplus of money in the West in the fall, after the crops are in, when things go right.

Senator BROOKHART. There are certain crops there now. Thank you.

The CHAIRMAN. Mr. Ottley is the last witness to-day.

STATEMENT OF JOHN K. OTTLEY, PRESIDENT OF THE FIRST NATIONAL BANK OF ATLANTA, GA.

The CHAIRMAN. Tell us something about your banking connections, besides being president of the First National Bank of Atlanta. You are connected with more than one bank, I understand?

Mr. OTTLEY. Yes, sir. I have that all in my statement.

The CHAIRMAN. You are telling your own business connections in the statement you are about to make?

Mr. OTTLEY. Yes, sir.

During a lifetime devoted exclusively to the banking business, I have always believed in national banks, and am still of the opinion that they should continue to furnish the soundest banking service to the country. I am in favor of every regulation that promotes their safety and stability without impairing their usefulness. I have always been an advocate of the Federal reserve system. So great was my interest and faith in the measure that I came to Washington to hear President Wilson deliver his message to Congress on the subject. In addition to aiding in its establishment I served for two terms as a director of the Federal Reserve Bank of Atlanta; am at present a member of the advisory council to the Federal Reserve Board, and have at all times aided in securing new members and in endeavoring to extend the usefulness of the system. This statement is made in no spirit of egotism but merely for the purpose of assuring the committee, who do not know me, that I appear here as a friend of the system you are endeavoring to perfect, and as one who desires earnestly to be permitted to round out his banking career within the Federal reserve system.

It is not my purpose to discuss this bill in its general application, but merely to show you how it affects the institutions with which I am associated, and it is, therefore, proper that I should describe them. The First National Bank of Atlanta has furnished sound and conservative banking service to its city and section for more than 65 years. It is the oldest national bank in the cotton States and the largest bank south of Philadelphia. Indorsed upon the certificates held by the shareholders of this bank is the usual clause evidencing their pro rata beneficial interest in the trustee stock of the Trust Co. of Georgia.

This trust company has been a member of the Federal reserve system for a great many years. It was one of the first trust companies established in our part of the South, and by its conservative management has acquired a valuable good will. Its capital stock is \$2,000,000. Its surplus is \$2,000,000. It has more than a million dollars of undivided profits, and it is administering estates and trusts or has wills on file representing something like \$100,000,000.

The First National Associates is a corporation organized under the laws of Georgia, all of whose capital stock is held by the Trust Co. of Georgia. None of it is held by the public.

This company owns the majority of the capital stock of the following national banks, located in the five largest cities in Georgia, outside of Atlanta: National Exchange Bank, Augusta, Ga.; Fourth National Bank, Columbus, Ga.; First National Bank & Trust Co., Macon, Ga.; First National Bank, Rome, Ga.; Liberty National Bank & Trust Co., Savannah, Ga.

The First National Associates is the owner of a large quantity of other property, but is strictly a holding company and does not engage in any active business whatever.

Under the various definitions of affiliates in section 2 of the act, it would appear that the First National Bank of Atlanta, the Trust Co. of Georgia, and the First National Associates are each affiliates of the other and of the national banks located in Augusta, Columbus, Macon, Rome, and Savannah. Surely it was not the intention to include member banks as affiliates. This would apparently follow from the fact that affiliates are required to make statements and submit to examinations which would be quite unnecessary if affiliates are member banks. The act can be made clear, if this is the intention, by limiting the term "affiliate" to trust companies, finance companies, securities companies, discount and acceptance companies, investment trusts, or other similar institutions or corporations not members of the Federal reserve system (top of page 2.) I submit for your consideration a proposed amendment to this effect.

Amendments to S. 4115: Page 2, line 1, after the words "trust company" insert the words "other than a member bank."

Page 2, line 4, after the word "corporation" insert the words "not a member bank."

Indorsements on stock certificates: The act, if passed, would compel us to do away with the indorsement on the present certificates of the stock of the First National Bank evidencing the ownership of the holders in a pro rata amount of the stock of the Trust Co. of Georgia, thereby completely divorcing the two institutions. (Sec. 17, p. 38, line 17.) Granting the power of Congress to do so, it seems to me that the power should not, under the circumstances, be exercised unless the necessity is compelling.

At the time this arrangement was made between the bank and the trust company it was entirely legal and in accordance with a long-established precedent which had at least the silent approval of Congress. For approximately 20 years such indorsement had been commonly used before it was adopted by our companies, and Congress had not sought to prohibit it. Rights had grown up under it, investments had been made on account of it, and the obligations of these contracts should not be lightly violated. A large amount of trust business which might have come to the bank has been turned over to the trust company, and these trusteeships can not now be altered.

If I may be permitted I would like to say at this point, I assume that it is probably known to all members of this committee that there have been court decisions, one in Massachusetts, and one in Georgia holding that a consolidated bank does not succeed to trust powers. We had a State bank in Georgia doing a trust business and a national bank, and we consolidated them, and immediately following the consolidation of those two under the national-bank charter, the national bank was enjoined from succeeding to the trust business of the State bank, and it was carried by us to the Supreme Court and the Supreme Court of Georgia affirmed the decision. That is what I mean by that.

The CHAIRMAN. In other words, you were sustained in your position?

Mr. OTTLEY. Yes, sir; that the trusteeships can not be changed.

I would like further to defend the practice itself. Instead of being a detriment to sound banking, it is, as we use it, in the interest of sound banking. Practically all the powers of the Trust Co. of Georgia are incidental powers of banking which the First National Bank has the right to exercise. Instead of having all these activities of a purely trust nature, carried on by the bank, they are exercised by a trust company of substantial character with a long-established reputation, itself a member of the Federal reserve system. The bank is thereby left free to devote all of its energies and capital to purely banking functions, which is, to my notion, in the interest of sound banking practice. At the very least an exception should be made of banks and trust companies which are members of the Federal reserve system and subject to the regulations of the board.

Group banks: The act would, in my opinion, have a disastrous effect on the group of banks in Georgia affiliated with the First National Bank of Atlanta. This group was organized in accordance with the law, and rights have grown up which could not be protected under the Federal reserve system if this act is passed. Each bank in this group is unquestionably stronger and able to afford better service to the public as a member of the group than it would be if operated independently.

As between group banking and branch banking under proper regulations, I have no hesitation in saying that I advocate the latter. Section 21 of the act, page 45, is an approval of branch banking, but it does not go far enough to save the groups already organized since it is limited to those States which permit branch banking by State law. Georgia permits branches but under such limitations and restrictions as would not be applicable to our group. The legislature of the State is not scheduled to meet for more than a year and we could not, therefore, reasonably expect to secure the necessary legislation in time to save our group unless this act is amended by permitting groups already organized to be converted into one bank with branches at the places where the established banks are now located.

All members of our group are national banks and, therefore, members of the Federal reserve system. They are operated by independent officers, and in every instance care has been exercised to retain the local boards of directors primarily interested in the welfare of their communities and the accommodation of commerce, industry, and agriculture in the contiguous territory. In addition to subscribing their full quota to the National Credit Corporation and aiding in every legitimate way the other financial institutions in Georgia, these banks have retained the confidence of the public and have been able during the depression through which we have passed to afford adequate banking facilities to their respective localities.

Having been organized in full compliance with the laws of both of State and Nation, valid contracts have been made and relationships have been established affecting extensive property rights. Having done no wrong and having committed no crime, I respectfully submit that we should not be punished because some one else has broken faith or abused a privilege. The many provisions of the act aimed at group banking would affect seriously not only our banks, which represent 30 per cent of the banking capital and deposits of Georgia, but also another sound and well-organized group in the same territory.

These two groups furnish to the commerce, industry, and agriculture of Georgia more than half of its banking accommodations.

Senator TOWNSEND. You are speaking of the whole State now?

Mr. OTTLEY. Yes, sir; the whole State.

The CHAIRMAN. Did I understand you to say this group furnishes the banking facilities for more than half the State?

Mr. OTTLEY. I say the group that I represent furnishes more than 30 per cent of the banking capital and resources of the State. There is another well-managed, sound, strong group, which, together with our group, furnishes more than 50 per cent of the banking capital and more than 50 per cent of banking credit of the entire State.

The CHAIRMAN. Inasmuch as you speak of capital and credits I will ask you, how many units does your group operate?

Mr. OTTLEY. Our group has the First National Bank in Atlanta and five units out in the State; in the five largest cities in the State outside of Atlanta.

The CHAIRMAN. You have six of the largest banks in the State?

Mr. OTTLEY. Yes.

The CHAIRMAN. And they furnish about 30 per cent of the banking capital?

Mr. OTTLEY. The other group has a larger number of units, even, than we have, though the total capital and deposits are not quite so large as in the group that I represent.

The CHAIRMAN. They have about how many units, as an estimate?

Mr. OTTLEY. I would say that they have approximately a dozen.

The CHAIRMAN. Are they organized on the same basis that you are? Is the set-up the same?

Mr. OTTLEY. I am glad you asked me that question. The other group is the Citizens & Southern National Bank with headquarters at Savannah, and they have branches in Atlanta and Augusta and Macon and Athens. Then, in addition to that—

The CHAIRMAN. Are they branches under the State law?

Mr. OTTLEY. Yes, sir. They took those branches when they were a State bank and the laws of the State of Georgia permitted branch banking. Then, when they joined the Federal reserve system, they retained those branches, but they got those branches under the State law.

Branches are not now permitted in Georgia outside the cities because somebody put in a rider on a bill in the Georgia Legislature one night after 12 o'clock. I was up there at the legislature until about 12 o'clock listening to the bank bill. It looked as if it was settled and everything, and then somebody after 12 o'clock stuck in a rider limiting the branch banking in Georgia. Since that time the other group, the Citizens & Southern National Bank, have established affiliates just the same as we have.

The CHAIRMAN. Who are the holders of the stock, then? Have they a holding company that is the holder of the stock of those affiliates?

Mr. OTTLEY. That is the way it is done in the State of Georgia. They must be held by a holding company.

The CHAIRMAN. How many of these affiliate banks have they, about?

Mr. OTTLEY. They have, for instance, established an affiliate at Dublin, which, I think, was the first one. That is a good-sized town

in which every bank in the town had failed, and upon the popular request of the people they went down to that place and established an affiliate.

The CHAIRMAN. Which affiliate has a national bank charter or a State bank charter?

Mr. OTTLEY. That one has a State bank charter. Then they have an affiliate at Thomaston. That is a State bank. Then they have an affiliate at La Grange, Ga., and that is a national bank. Part of their affiliates are national banks and part of them are State banks.

The CHAIRMAN. Their total number of units would not be over 15 or 20 branches and affiliates?

Mr. OTTLEY. No.

The CHAIRMAN. That is what I am trying to get at. I was not sure that I understood your set-up. I understand a number of large banks have the stock held in a holding company there.

Mr. OTTLEY. The stock is held by our holding company; yes, sir.

The CHAIRMAN. All right. I thank you. You may proceed.

Mr. OTTLEY. These two groups furnish to the commerce and industry of Georgia more than half of its banking accommodations. A way out should be left open, and this is through branch banks. Groups already organized should be permitted to retain as branches the banks they now have, notwithstanding the State law.

Senator GLASS. I understood you to say Georgia permitted branch banking.

Mr. OTTLEY. Senator, I said that at one time Georgia permitted state-wide branch banking. It now permits branch banking but in a limited way and so limited, in fact, that it would not cover the case of either the First National group or the Citizens & Southern.

Loans on collateral security: The term "loans on collateral security" used in many places in the act should, in my opinion, be clearly defined and limited. Loans on warehouse receipts, compress receipts, bills of lading, and paper that stands for commodities of all sorts are loans on collateral security. Banking accommodations can not be afforded to the commerce, industry, and agriculture of the country without loans on collateral security.

Under section 18 of the act, page 39, line 16, no national bank or member bank can perform the functions of a correspondent bank or have as its correspondent any corporation that makes loans on collateral security. Since all member banks make loans on collateral security, none of these could act as correspondents for any other or have any other act for it, and this prohibition would apply to the Federal reserve banks themselves since they likewise make loans on collateral security. I am sure this was not intended, but there is no escape from the plain language of the act. If a certain kind of collateral security was intended this should be defined and all other collateral loans excluded.

One hundred dollars par value: Section 17 of the act, page 38, restores immediately the par value of all national-bank shares to \$100 each, but gives to banks having shares of less than \$100 par two years within which to issue new certificates. While I have no objection to this change if it can be brought about without affecting the present rights of stockholders, I call attention to the fact that all persons having less than \$100 par value of stock are automatically

disfranchised. If the par value at present is \$10 a share and a shareholder has less than 10 shares, he could not vote and there would be no way to issue him a certificate. Under those circumstances what would become of his double liability? If the banks must issue new \$100 par certificates it is only fair that the act should provide a method by which it can be legally accomplished.

Unobjectionable provisions: There are many provisions of the act to which I personally have no objection, among them the open-market committee and the requirements as to reports and examinations of affiliates. The more frequent and the more searching you make the examinations of the institutions in which I am interested the better pleased I will be.

I heartily indorse the provision of section 28 for the removal of an officer or director for the continuance of unsafe and unsound practices, and I believe that the enforcement of this provision would strengthen the banking system of the country. I can not emphasize that section too strongly, because it is familiar to every member of this committee that banks have gone along with mismanagement and the public has known about it, and the Comptroller of the Currency has known about it, and the superintendents of State banks have known about it and they have criticized it. But the way to get them out has not been plain, and I think that a way ought to be made to get them out; and so far as I am concerned as a banker, I willingly and heartily indorse that section.

Senator BROOKHART. I would like to apply that to the Federal Reserve Board itself.

Mr. OTTLEY. If I do not do right I am ready to let any three people vote on me.

The CHAIRMAN. I think you want to go ahead without much interruption. It is getting late and I hope you will be permitted to.

Mr. OTTLEY. I am nearly through.

While I have no particular interest in the restrictions sought to be placed on 15-day loans, section 11, page 25, I am of the opinion that the effect will be to limit a facility which is much needed to deprive the Federal reserve banks of a profitable business, and to lessen the value of Government securities.

Real-estate loans: Attention has been called by others to the practical difficulties involved in the enforcement of the provisions of section 14 of the act, page 33, relative to the revaluation of all real-estate loans and the adjustment of the loans to the revised valuations. I indorse the testimony already given by others on this subject, and would merely add that in my opinion this provision would prevent national banks from making form loans, and would give to the insurance and loan companies a monopoly of this business.

Increased reserves, section 13, beginning on page 27: I have devoted my exclusive attention to banking during my entire business life, and I give it as my deliberate opinion that character of assets and not lack of reserves has been the cause of bank failures. The increase of reserves at the present time is unwarranted, uncalled for, contrary to the best interests of the banking system of America, and lessens the ability of the banks to accommodate commerce, industry, and agriculture.

The Federal reserve banks do not need these additional funds. The member banks do need them. The First National Bank of

Atlanta alone has \$28,000,000 in time deposits, mostly in the savings department. The additional reserve on this sum would amount to \$1,960,000. In other words, my bank would have just that much less to lend its customers and just that much less to stimulate the commerce, agriculture, and industry of the section in which it operates.

As a banker I would estimate this money as having an annual earning value of 5 per cent or \$98,000. Our bank has reduced its dividend rate 25 per cent. Twice the salaries of its officers and employees, beginning at the top, have been reduced. Other necessary economies in operation have been put into effect, and, in the face of all this, to suffer the loss of \$98,000 a year in revenue is more than we should be asked to bear. The fact that we are given five years to accumulate this additional reserve affords little comfort since the obligation is immediately established.

Under the proposed reserves a nonmember State bank in Georgia with the same deposits as the First National Bank of Atlanta would have a possible advantage of \$225,000 a year in earnings, since the reserves of a member bank must be carried in the Federal reserve bank without interest, while a nonmember bank could invest its reserves in United States or State bonds.

Investment and segregation of time deposits, section 14, page 32: Section 14 makes it mandatory for national banks to invest all time deposits not loaned upon the security of real estate in an eligible list of securities set up under the State law in which savings banks may invest, or where there is no such law, in such property and securities as may be specified by the Comptroller of the Currency. (P. 33, line 22.)

The section further provides that all the property of any insolvent national bank acquired under this section shall be applied by the receiver thereof in the first place to the payment in full of its time deposits. (P. 34, line 11.)

Since real estate loans are made impractical under the provision for revaluations and readjustments, it will mean that all time deposits must be invested in securities approved by the State for the investment of savings bank funds, or in such property and securities as may be specified by the comptroller, and they will thereby be withdrawn from the available bank credits to commerce, industry, and agriculture. This in my opinion is the exact reverse of what should happen. We need in this country more liquid bank credits. There are enough frozen assets already. We need money to handle the crops, to hold them, if necessary, for better markets, and to carry on the general legitimate business enterprises of the country. In my own bank we have approximately \$75,000,000 of deposits, of which \$28,000,000 is classified as time deposits. If this act becomes effective, none of this money—which means \$28,000,000—can be used for commercial banking purposes or the accommodation of commerce, industry, and agriculture. When the average depositor learns that his time deposits are additionally secured, we may confidently expect that he will resort more and more to time deposits, leaving only a necessary balance in his checking account so that the time deposits may soon come to exceed by far the demand deposits in national banks. This provision of the act applies only to national banks. By reason of the lien given time depositors, the demand

deposits will become to that extent more insecure. Since depositors in State banks in Georgia and probably in most of the other States stand on an equal footing, it becomes apparent that time deposits will enjoy the greater security in national banks and demand deposits in State banks. The inevitable tendency will be to encourage the use of State institutions for commercial banking and to transform national banks into savings associations.

The CHAIRMAN. I am not sure that I understood: Is there a double liability in the stock held in your holding company?

Mr. OTTLEY. There is not a double liability; no, sir. But, as I stated, we have a large amount of property other than bank stocks.

The CHAIRMAN. I am simply trying to find out how many of these bank groups retain the double liability feature of the unit bank. I thank you.

The committee will meet at 10.30 o'clock to-morrow morning in the regular committee room.

(Whereupon, at 6.40 o'clock p. m., an adjournment was taken until Tuesday, March 29, 1932, at 10.30 o'clock a. m.)

OPERATION OF THE NATIONAL AND FEDERAL RESERVE BANKING SYSTEM

TUESDAY, MARCH 29, 1932

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10.30 o'clock a. m. in room 303 Senate Office Building, pursuant to adjournment on yesterday, Senator Smith W. Brookhart presiding.

Present: Senators Brookhart (presiding), Townsend, Fletcher, Glass, Wagner, and Bulkley.

Senator BROOKHART (presiding). The committee will come to order. We will hear Mr. Preston first.

STATEMENT OF THOMAS R. PRESTON, CHATTANOOGA, TENN., PRESIDENT OF THE HAMILTON NATIONAL BANK

Mr. PRESTON. Mr. Chairman and gentlemen of the committee, I have not prepared a statement although I have a few notes of what I hope to say. I shall attempt to make clear to the committee how this bill would affect our institution, and I think what will affect one would affect all.

I am not going to attempt to speak except on two or three points. And I do wish to say that I believe the bill has many constructive features.

First, I am going to attempt to explain to you how the proposed reserve on time deposits would affect our institution. We have normally about \$20,000,000 of deposits, which are about 50-50; that is, half time deposits and the other half checking or demand deposits.

Our normal reserve is about \$1,000,000. In addition our deferred credits will amount to about \$500,000 more. So we have in reserve account and in the deferred credit account with the Federal reserve on the average about \$1,500,000 all the time.

Now, if the reserve is to be moved up on time deposits from 3 to 7 per cent it will mean that we will have to have \$400,000 additional.

In addition to that I will say that we are not in a reserve city, and we require a good deal of vault cash for pay rolls and other purposes. Our vault cash now is just about in the same proportion it was before the establishment of the Federal reserve system. So in reality with a bank no larger than ours one would have to have a reserve account of \$1,400,000 and deferred credits of \$500,000.

Now, if we may say that money is worth 6 per cent, and that is the legal rate in Tennessee, it would cost our bank \$24,000 per annum additional.

I appreciate the fact that the Federal reserve system is rather an expensive thing. It has many advantages, of course, and this thing of switching deposits from demand to time will be an expense to us, too, which will be more than we could gain.

For instance, when we pay interest on demand deposits at all it is at the rate of $1\frac{1}{2}$ per cent, and on savings we pay $3\frac{1}{2}$ per cent. So there is a difference of 2 per cent, and all that we would save would be the difference between \$30 on each \$1,000 and \$70. So instead of being an advantage to us it would be an expense.

I will say that we have rarely ever switched checking accounts to savings accounts.

Senator BROOKHART. How about the case of other banks; would that be an expense to them if they did that?

Mr. PRESTON. It would be the same probably to all banks.

Senator BROOKHART. Then why do they do that switching?

Mr. PRESTON. In our section of the country they do not do it to any extent. Of course I can not speak for other sections, and I can not speak for the other fellow, but I will say that we have never done it to any extent. Occasionally we have had temporary deposits that we have switched, but it is very seldom the case. In fact, at this time I can not recall a single account that we have of that kind.

Another thing about the Federal reserve system, the people are not sold on the system. A sign up on a bank that it is a member of the Federal reserve system, to the public, does not mean what it should mean. In other words, I do not think we have many, if any, customers who do business with us because we are a member of the Federal reserve system, or who would quit us if we were not.

To put this additional burden on us would right at this time be a hardship. We have reduced dividends. We have reduced expenses. We have reduced the pay of everybody from the porter up. And this would mean to us in the matter of reserve an expense of \$24,000 per annum.

Senator BROOKHART. On that switching business I can see if they switch from demand to time accounts, which would mean that they would only pay the demand rate, where they would gain an advantage by reducing the reserve.

Mr. PRESTON. You take these bank examiners, and they would be pretty apt to find that out and report it. I do not know that many banks do that, because the difference between the time rate and the demand rate is quite considerable. On lots of accounts we do not pay anything at all.

Senator BROOKHART. Is there any way that it could be stopped without increasing the time reserve?

Mr. PRESTON. Yes. I think the bank examiners could stop that.

Senator GLASS. But the bank examiners do not seem to have stopped many things that went on in Tennessee and Kentucky some time ago.

Mr. PRESTON. Well, that is true.

Senator BROOKHART. You may proceed with your statement.

Mr. PRESTON. Another thing, eligible paper in banks is growing less all the time. There are many reasons for that situation, but one reason is that the average Federal reserve bank is rather drastic in their consideration of what is eligible paper. And then, too,

improved transportation facilities has had a good deal to do with reducing the amount of eligible paper.

We, as a rule, are a nonborrowing bank. We seldom use eligible paper, and do not believe much in rediscounts and bills payable except for temporary purposes and emergencies.

Now, you take this liquidation corporation that has been proposed, and I think upon the whole it is a good thing. I think it would inspire confidence to some extent in the public. If the bill is enacted as drawn our subscription to the stock of such a corporation would be \$100,000, and I am very doubtful if that stock would ever pay us anything in the shape of dividends.

Usually a bank exhausts its good assets before it fails. In liquidation there is very great depreciation. Now, that contribution coupled with the excess reserve would cost our institution \$30,000 a year figuring money at 6 per cent, and about a like amount for the banks that we are associated with or in a measure own. So upon the whole it would cost us and our associates, and I will come to that in a minute, \$60,000 per annum, which would be a very great hardship at this particular time.

Now, in a sense the subscription to this proposed liquidating corporation means you will be doubling on the banks in a way. You make them put up one-half of one per cent on their deposits, and then the Federal Reserve System contributes to it. The Federal reserve makes very little money except upon the accounts the banks keep and the stock.

Now, I will say that we have a subsidiary which has a capitalization of \$500,000, which was created by dividends. The certificate of the Hamilton National Bank carries with it a proportionate interest in this subsidiary. This bill would completely put that institution out of business and force us to liquidate what we have.

And why should that be done? We think we have been constructive along that line. We handle municipal bonds, a few industrials, and some preferred stocks. I can cite one instance in which I think we have been helpful through that subsidiary to our community: Our city water company, which is not publicly owned, wanted to extend their mains. In connection with another institution in our town we underwrote \$500,000 of preferred stock of the water company and sold it to the public, and thus the water company extended their mains. And that is one stock which this depression has not depreciated to any extent. It is being redeemed as agreed, and the interest is promptly paid.

As I view the situation, people will always invest in securities. I think a subsidiary of a bank as a rule is as responsible as the average individual broker. Some in our town are responsible and others are not, and to those the investing public would be driven.

Senator BROOKHART. Do you invest in listed bonds on the stock exchange in your bank?

Mr. PRESTON. To some extent but to a very limited extent.

Senator TOWNSEND. Do you favor the same examination for your affiliate?

Mr. PRESTON. Yes, sir. I see no reason against it. As a matter of fact we have an examination now of the affiliate the same as of the bank. An examiner has just completed an examination of our institution, and he examined the affiliate the same as the bank.

Senator TOWNSEND. Referring back to the matter of the reserve, do you feel that the present reserve is adequate?

Mr. PRESTON. I think so. I do not see why it is not, I do not see why the Federal reserve system needs any more money, and it lessens the lending power of a bank when you increase the reserve, there is no question about that.

Senator BROOKHART. You may continue your statement.

Mr. PRESTON. Now, as to these 15-day loans: We sometimes use that 15-day privilege but I do not recall many instances when we have used it, and it has not always been on Government securities. And it is quite an advantage to us. While that is not important, I mean that extra 1 per cent, still it would be a hardship on us and a hardship on the community.

Rediscounts and bills payable in our section of Tennessee have never been popular.

Now, as to the rate of interest on loans: Our rate in Tennessee is 6 per cent, and, in this bill it says that the rate of interest must never exceed the legal rate. In my judgment that will do harm to the very people it is intended to benefit, and they are the small borrower at the country bank. A man in Tennessee who borrows \$50 from a small country bank, which is one of these character loans we talk about, would be charged under this bill 25 cents. As a result they won't make any loans.

Now, the industrial loan people, the Morris Plan Bank and others, in our community charge 16 per cent, and I think they are doing a very constructive and helpful work. If a man borrows \$100 they charge him 8 per cent and give him \$92, and give him 12 months in which to pay it, in 12 equal installments. By that plan he keeps all the money an average of six months which is 16 per cent.

That is the lowest of those rates I know anything about in our community.

If you eliminate the little follow from the making of character loans, you will drive him to the industrial banks or to the loan sharks.

Senator GLASS. Mr. Preston, it seems to me you have an amazing misconception of that provision of this bill.

Mr. PRESTON. I may misunderstand it.

Senator GLASS. You are not permitted now to charge more than the legal rate of interest, are you?

Mr. PRESTON. Yes, we charge the legal rate of interest.

Senator GLASS. That is what I say. The purpose of that section of this bill was to—

Mrs. PRESTON (continuing). But it is not enforced. But the most of our loans are at the rate of 6 per cent.

Senator GLASS. I do not think any restraining statutes about banking are enforced. That is the trouble. But I am saying that you have the legal limitation now.

Mr. PRESTON. Yes.

Senator GLASS. The sole purpose of this bill was to allow you to charge above that legal rate when the Federal reserve bank raises its discount rate, so that you will not be precluded altogether from transacting business in such times. For example, in 1920 the rate at three Federal reserve banks was raised to 7 per cent. It was raised to 7 per cent in those territories where a majority of the States had a

legal limitation of 6 per cent. Your bank in those circumstances could do no rediscounting at all except at a loss of 1 per cent.

Mr. PRESTON. We could not.

Senator GLASS. Well, the whole purpose of that section would be to enable a bank to do it in those circumstances.

Mr. PRESTON. Well, I did not so understand the provision.

Senator GLASS. I see you did not.

Mr. PRESTON. I am glad to know it. I thought it limited a bank's character loans to the legal rate.

Senator GLASS. It enables a bank in such circumstances as I have described to increase its interest charge, and that was the whole purpose of the provision.

Mr. PRESTON. Thank you.

Senator BROOKHART. You may continue your statement.

Mr. PRESTON. Now, we have a small group, and under the terms of this bill—well, I will first describe the group: We have a group only in our immediate territory. The parent bank is one and there are 16 others. Our total deposits normally are about \$40,000,000. There are 4 groups in Tennessee, 2 in Nashville, 1 in Chattanooga, and 1 in West Tennessee, composed wholly of country banks. Not a single one of those banks has had any trouble during this depression, and I will say that I have been in the banking business a good many years, and have gone through five depressions, but I have never seen values melt as they have during this time. The depression of 1893 was bad, but not as bad as this. None of these banks has failed or taken the 60 days' withdrawal notice, and I think all of them have done constructive work, and they have saved a good many weak banks. We have ourselves taken over six in the past year and a half, and some of those I know would have failed.

Another thing we have found, and I think it is true of all sections of our State: The public are not against branch or group banks. They like to do business with a large and sound bank.

Senator GLASS. Well, they are not the same thing, Mr. Preston.

Mr. PRESTON. I know they are not the same thing.

Senator GLASS. They are not the same thing by any means.

Mr. PRESTON. But the public have no objection to either kind so far as I have been able to ascertain.

Senator GLASS. We have been urged to abolish group banking altogether.

Mr. PRESTON. Well, I think it is all right to abolish group banking if we had some place to go.

Senator GLASS. Well, we have tried to provide you a place in this bill to go, in the matter of branch banking.

Mr. PRESTON. Branch banking would be all right. The bill provides that we can go to branch banking only when the State laws allow the same privilege to State banks. As an example, you gentlemen would follow the Tennessee Legislature, and it looks to me like it would be fairer for the Tennessee Legislature to follow Congress.

Senator TOWNSEND. Doesn't the State of Tennessee permit branch banking?

Mr. PRESTON. Only within city limits.

Senator GLASS. If it permits it at all under this bill a national bank would not be confined to a State. We do not require that.

Mr. PRESTON. You permit only state-wide branch banking or area-wide branch banking when the State permits it.

Senator GLASS. Yes.

Mr. PRESTON. Then some national banks in some States would have a state-wide privilege, while in Tennessee they would not have it. It may be all right, but I don't just quite understand the provision.

Senator GLASS. That might put you to the necessity of going to the Tennessee Legislature and getting them to legislate on a sound basis for branch banking.

Mr. PRESTON. It would.

Senator GLASS. But if you can assure us that Congress will make it otherwise we will be very glad for you to do it.

Mr. PRESTON. It looks to me like these limits could be put on branch banking. For instance, you could have the groups covert their units into branches and stop there, or you could permit them to extend their branch banking when they bought out an older institution and allow them to go on.

I think the unit bank has served a great purpose, and that it should be preserved and protected. I do not believe that a large bank should be allowed to put up a branch in any community at will. They might buy an old bank or something like that or absorb one and create a branch.

Senator GLASS. Did you ever hear of a borrower at a bank, a business man or merchant, who wanted credit at a bank, who objected to branch banking?

Mr. PRESTON. In few instances I have.

Senator GLASS. I never have.

Mr. PRESTON. In fact, most complaints come from the borrower.

Senator GLASS. Well, I have been in Congress 30 years, and I have sat in at many bank hearings, and I have never known a man who wanted credit, who was a borrower at a bank, to object to branch banking.

Mr. PRESTON. It is seldom the case, that is true.

Senator BROOKHART. I can bring you some that will make very emphatic objections out of their own experience.

Senator GLASS. They might be major stockholders in some bank who wanted to monopolize the community.

Senator BROOKHART. No; they are not bankers at all.

Mr. PRESTON. I think the key to this whole business is the branch banking feature if it is extended and you allow these groups to convert. I think that will do as much to stabilize the financial situation as anything else, and probably more than anything else I know of.

Senator BROOKHART. In branch banking doesn't it often turn out that the local branch has to get authority from a higher place?

Mr. PRESTON. Sometimes that is true, but that depends upon managers.

Senator BROOKHART. And it is very detrimental to the local community.

Mr. PRESTON. Sometimes that is true. And sometimes it would be better if it were true more frequently, to have at least a conference about loans.

Senator BROOKHART. You may proceed with your statement.

Mr. PRESTON. Well, that is about all I have to say, gentlemen of the committee.

Senator BROOKHART. Any more questions? (A pause, without response.) We thank you, Mr. Preston.

Mr. PRESTON. I thank you gentlemen for hearing me.

Senator BROOKHART. We will now hear Mr. Payne.

STATEMENT OF WILLIAM K. PAYNE, CHAIRMAN OF THE BOARD, AUBURN-CAYUGA NATIONAL BANK & TRUST CO., AUBURN, N. Y.

Mr. PAYNE. Gentlemen of the committee, I come here as a small-town banker in a small city in the State of New York, in the heart of the agricultural section, where a good deal of our business is dependent upon agriculture and the success of agriculture. A good deal of our business is done with farmers.

Senator BROOKHART. Is that in northern New York?

Mr. PAYNE. No; it is in central New York, west of the central part of New York State.

Our bank is a merger of two banks, one of which had served the community for 115 years and the other for 99 years.

We have been through a great many depressions, and we hope and expect to get successfully through this depression.

I appreciate that this committee has been engaged in a long and exhaustive study of the banking situation, and I think you are entitled to the gratitude of all bankers for your work, and I certainly do not want to come down here to Washington with any captious criticism of any of the features of this bill.

But I, as well as other bankers in my section, are seriously alarmed because of the very earnest belief that any attempt to change materially existing banking and commercail practices at this time will tremendously handicap the recovery of business and the prosperity of our people up there.

During the last 10 years I have had considerable to do with the so-called banker-farmer movement up in our section of the country, and I think I know considerable about the attitude of the small-town banks in relation to our agricultural community and what their troubles are. And I might add that we are having a very real struggle to keep the people there going, and we feel that they want and need all the help we can give them.

Senator BROOKHART. Do you have many abandoned farms in your section of the country?

Mr. PAYNE. A considerable number. We have a reforestation project up there that is going to take care of many of those farms. It will cost a good deal of money, but ultimately I think it will solve some of our farm problems up in that whole section of the State.

As a small-town banker I have little immediate interest in the so-called affiliates. Many of them seem to be serving a useful purpose, and some of them seem to have been operated not entirely for the public good. The sort of banks I am speaking for are not bankers for stock exchange brokers or investment banking houses. At the same time, we do feel with a strong conviction that an attempt at this time to "reform drastically," if you please, this branch of our financial system, in the manner proposed by this bill, would so

inevitably and seriously affect security values that many of our small country banks, which have so far successfully weathered the storm, would not be able to survive.

Senator BROOKHART. Do you mean by that statement that country banks buy a good many of these securities?

Mr. PAYNE. Yes; altogether more than we wish they had.

Senator BULKLEY. What provision of this bill will hit securities?

Mr. PAYNE. By disturbing or throwing out of gear this system of marketing and carrying securities through the banking system.

Senator BULKLEY. I do not quite follow you yet. What will do that?

Mr. PAYNE. This idea of cutting off from the facilities of commercial banks those people that are engaged in investment banking or stock exchange houses, it would inevitably throw on the market in a very chaotic way a lot of securities.

Senator BULKLEY. Your understanding is that the bill cuts them off from the facilities of banks?

Mr. PAYNE. I think it would severely hamper the existing system.

Senator BROOKHART. That ought to have been done before those country banks bought those securities.

Mr. PAYNE. Possibly so. I am not particularly interested in how they do business, but I am very much interested that the present system shall not be disturbed, certainly not at the present time, speaking from a selfish standpoint, for I believe it would affect our own securities.

Senator BROOKHART. If it is wrong, it seems to me we have got to get rid of it.

Mr. PAYNE. What was that?

Senator BROOKHART. I say, if it is wrong at some time we have got to get rid of it.

Mr. PAYNE. Yes. And of course there are a great many changes that could be made in the law at the proper time. But we are in a situation now where we are very much alarmed at the idea of these things being done, just at the present time.

Senator BULKLEY. I do not think you have made clear how this is going to hurt that situation any.

Senator TOWNSEND. Is it your feeling that any bill passed now would be dangerous to the situation you have described; is that your idea?

Mr. PAYNE. Yes. Any bill that markedly changes the existing situation, a situation which has grown up, of course, through an experience of years, would materially affect us in these present times. And the situation to-day is so delicate that any little thing, such as the suicide of Mr. Ivar Krueger in Paris, will have a bad effect. That had a tremendous effect. I know a bank that has some of those securities.

Senator BULKLEY. How much influence in the matter of actual points of depreciation did that suicide have?

Mr. PAYNE. How was that?

Senator BULKLEY. How much effect did it have?

Mr. PAYNE. Well, I know of one bank that had quite a lot of their securities, that they have wanted to get rid of for a long time but have not had the courage to take the loss, and they are seriously contemplating whether they will not have to close.

Senator BULKLEY. What does that have to do with the fact of the suicide?

Mr. PAYNE. Well, the market went down.

Senator BULKLEY. How much?

Mr. PAYNE. I can not quote you the figures.

Senator BULKLEY. Very little, wasn't it, and it came right back again?

Mr. PAYNE. It was quite a lot.

Senator TOWNSEND. The Krueger and Toll securities were affected tremendously.

Senator BULKLEY. In the matter of their securities, yes; but I thought Mr. Payne was talking about the general market situation.

Mr. PAYNE. I say that one thing disturbed that section of the market, and there is one bank I know of that will quite likely have to close by reason of it. And if there is another general disturbance, or other disturbances of the market at the present time, it will add to the troubles of the banks.

Senator BULKLEY. I do no see that you have pointed out any disturbance that would be created by this bill.

Mr. PAYNE. Well, I think it is quite evident that if the provisions of this bill drastically change the banking situation at this time, that will be the result.

Senator BULKLEY. What do you mean is so drastic? What point about this bill is drastic?

Mr. PAYNE. It would affect banks in many ways. You are cutting them off from the use of commercial banks. I mean people engaged in financing securities.

Senator BULKLEY. What provision of this bill cuts any person off?

Mr. PAYNE. You are providing, for instance, that investments in banks on time money shall be limited to certain real estate and savings bank securities.

Senator BULKLEY. What provision of the bill are you referring to now? I am not quite sure that we are talking about the same thing?

Mr. PAYNE. It is section 14, I think. [Reading:]

Every such bank may apply the moneys deposited therein as time deposits to the loans herein authorized, and the balance of such time deposits—

Senator BULKLEY (interposing). On what page of the bill do you find that?

Mr. PAYNE. Page 33, at the bottom of the page.

[Continuing reading:]

and the balance of such time deposits shall be invested in property and securities in which savings banks may invest under the law of the State where such national bank is situated.

Now, there are—

Senator BULKLEY (interposing). How much difference does that make in the case of your bank now?

Mr. PAYNE. To my own bank very little, but I know of a bank, that has securities and they are just holding on by their toes.

Senator BULKLEY. You are speaking now about real estate securities.

Mr. PAYNE. No; I am speaking about the same securities that they have now, but they are not savings-bank securities.

Senator GLASS. Ought they to have them?

Mr. PAYNE. No. But this is a time when they are almost dead, and I do not think you should suffocate them.

Senator GLASS. When will we stop it with the bad kind of bank?

Mr. PAYNE. When the situation gets so there is a real market for securities, founded on their intrinsic value, and not when prices are founded on panic values, such as we have now.

Senator GLASS. Then won't the bankers come here and say: Don't touch anything now. You will freeze this remarkable prosperity we are enjoying.

Mr. PAYNE. I will not, Senator Glass, because I think it ought to be done then.

Senator BROOKHART. I have a chart made by the Alexander Hamilton Institute which shows that stock values are right now as high as they were at the time of the 1919 war inflation.

Mr. PAYNE. Of course, our bank has no stocks. We are not doing a stock business.

Senator BROOKHART. Well, bonds would be inflated along with stocks, or at least they always are.

Mr. PAYNE. Well, we have a good many bonds in our bank that certainly are not inflated.

Senator BROOKHART. There are a good many bonds that are deflated.

Mr. PAYNE. What was that?

Senator BROOKHART. Isn't the trouble with bonds that the banks have purchased, they were inflated bonds and they are now depreciated in value?

Mr. PAYNE. Yes; perhaps that is so in some cases.

Senator BROOKHART. And if their value is less, somebody has got to take the loss. Should we give them the opportunity to pass that loss off on to innocent people?

Mr. PAYNE. I think at this time, Senator, if we should do that if we should close these banks by that action, it would do more harm to the investor than any possible harm that could be done by holding on to them until we get back to fairly normal conditions. In a small town if there is a bank failure it is a tremendous thing to the community, as you know.

Senator BROOKHART. I know that perfectly well. I have been in two of them myself, so that I know from experience.

Mr. PAYNE. Well, right around my section we have not had any, and we certainly don't want any.

Senator WAGNER. Mr. Payne, has there been a shrinkage in the amount of loans made by your bank covering, say, the last 12 months?

Mr. PAYNE. Yes. Of course we are not lending anything for the purpose of investment. Where people want to get into the market we don't help them. But people who have business loans, of course they have shrunk because they have not the use for the money. Many of our industries are not operating.

Senator WAGNER. That is the point I want to come to next. Is that due to the refusal of the bank to make loans?

Mr. PAYNE. Oh, no.

Senator WAGNER. Or is it simply the reduced demand for credits?

Mr. PAYNE. We would be very glad to make some good loans. We are loaning.

Senator WAGNER. That is due to business activity?

Mr. PAYNE. Yes. We are now loaning to some of our farmers who are looking ahead for their summer requirements, and even, I think, we are making some loans I do not like to make but I feel we have got to do it to help them along.

Senator WAGNER. Are they dairy farmers?

Mr. PAYNE. There are dairy farmers. We are a very diversified agricultural industry. We are on the edge of the fruit belt. We made a loan the other day to a man who has a large apple orchard as well as other things. We have diversity of products. Our country used to be the largest timothy hay county in the United States before Mr. Ford put the horses out of business. They have changed into dairying and raising of alfalfa and diversified crops.

Senator WAGNER. Do the farmers you are in touch with include the territory around Orleans County?

Mr. PAYNE. No. That is quite a little west of us. We are just 26 miles west of Syracuse.

Senator WAGNER. There were a number of bank closings in the Orleans district, were there not?

Mr. PAYNE. Yes; I think so. I am not very familiar with the details of it, but I know they had troubles up through there. They had some trouble in the fruit section. When the joint stock land banks started they made some very liberal loans up through there and got the farmers very badly in debt, and they have had a lot of trouble. We have had very little of that in our section.

Senator WAGNER. Some of the farmers up in that section now feel there are not enough banking facilities there for their purposes?

Mr. PAYNE. They may not have for the immediate time, but I think one of the things we are suffering from is they had too much credit. They were encouraged to borrow too much money some years ago.

Senator BULKLEY. I would like to understand further what you think is drastic about this. As I understand it, you are reading from section 14 as an example of a drastic change. Do you mean that it is a drastic change in the existing law to have this limitation on loans on real estate?

Mr. PAYNE. No; I do not think, Senator, that you understand me.

Senator BULKLEY. Just what is drastic about that? I would like to understand you.

Mr. PAYNE. I stated that thing would cause trouble to some of our banks. What I meant was—

Senator BULKLEY. What sentence in it would cause trouble?

Mr. PAYNE. It was not that paragraph that I referred to as a drastic change in industrial machinery. What I referred to particularly was the provisions in here. I have gone over this.

Senator BULKLEY. What was your purpose in referring to this paragraph? Do you object to it at all?

Mr. PAYNE. Yes. That a good many of our banks if they are limited to savings-bank investments suddenly will have to—

Senator BULKLEY. Limited to what? Limited to 50 per cent of their time deposits on real estate?

Mr. PAYNE. Limited to the balance that they may have in other than real-estate loans, to savings banks, to legals. It will compel

them to throw out of their banks at a very low price some securities that they have to hold on to in order to weather this thing.

Senator BULKLEY. You noticed how long a time they are given to complete by this section, did you?

Mr. PAYNE. Yes. If we knew when this recovery was coming, and how fast, we might not be so thoroughly alarmed; but in my opinion, and, I think, the opinion of most bankers, it is going to be very, very slow.

Senator GLASS. Suppose we advance the time from two to five years?

Mr. PAYNE. I think that would help very much.

Senator BULKLEY. I am inclined to think you are right about that. What did you mean by a drastic provision?

Mr. PAYNE. As I went over the bill I was impressed very much with the idea that it was going to very seriously cripple the—

Senator BULKLEY. That is very interesting, because quite a number of witnesses here have made the statement that some provisions of the bill are very drastic, and always when I ask them just what the drastic provisions are, we have this same long pause, which is not always shown in the record. I was wondering if you were going to be more successful than some of those.

Mr. PAYNE. That is all very proper criticism, Senator; but I confess that I was focusing my attention more on certain specific things here. I am not intimately interested in this stock exchange branch of banking; but going over the bill, without specifically making notes on just what they are, the impression was very strong on me it was going to interfere seriously with that business.

Senator BULKLEY. My theory is some of you gentlemen have had certain very drastic language suggested to you and you have adopted it without analyzing it for yourselves.

Mr. PAYNE. I have had no language suggested to me.

Senator GLASS. Either that or there is a coincidence of opinion and criticism that is rather extraordinary.

Mr. PAYNE. Well, it may be some of both. I do not know.

Senator GLASS. Some people have gone to night schools.

Senator BULKLEY. Just to get it fairly stated: Do you really mean that there is anything drastic in it, or was that just a general statement?

Mr. PAYNE. That was the impression made on me very strongly.

Senator BULKLEY. If it made that impression it surely ought to be justified by some one or more things in the bill.

Mr. PAYNE. It certainly should, and I confess that just at the moment I cannot put my finger on them. I am quite sure they are here.

Senator FLETCHER. The expression "a drastic provision" is a very general expression. What do you mean by "a drastic provision"? Restrictions or lack of restrictions, or what do you mean?

Mr. PAYNE. I mean a rather drastic interpretation of the methods of doing certain forms of business which have grown up for years and any change in which would be sharp for the time being, and that this is not the time to do anything of that sort.

Senator FLETCHER. You refer to the general effect of the legislation?

Mr. PAYNE. Yes.

Senator TOWNSEND. Is there a general opinion among the bankers in your section that any legislation now, whether drastic or mild, would affect the situation?

Mr. PAYNE. I talked with several of them before I came down here, and they all felt about the way I do, that this was no time to do it. We are under a severe strain, and we feel that anything that adds to that strain now simply should not be.

Senator GLASS. Then you think it would be deplorable for Congress to pursue this proposed investigation of the stock exchange right now, do you not?

Mr. PAYNE. I do not know as it would be, no. I do not think an investigation would do any harm—a constructive investigation.

Senator GLASS. Do not you think that would be rather disturbing right now?

Mr. PAYNE. Well, we have had so much, if it is not followed by a threat of immediate action, I doubt if it would have a serious effect. I am not an expert on stock exchange procedure and my opinion is worth very little on that subject, Senator, if anything.

Senator GLASS. But you seem rather disturbed over what you think is some drastic interference with that.

Mr. PAYNE. I mean as it affects us as small country bankers. As far as the large bankers are concerned, that is their grief. I do not want to speak for them. I do not know about their situation.

Senator BULKLEY. It is not too late, if we can find something that is really drastic in the bill, to correct it, but if you can not guide us to it and we can not think of anything ourselves, it is pretty hard to make it less drastic.

Mr. PAYNE. I got in here yesterday and heard some of the addresses here, and I have read some of the newspaper reports, and it seems to me that—

Senator BULKLEY. Have you heard anything more than just a vague generality about how drastic it is?

Mr. PAYNE. I think I have. I do not know what you mean by a vague generality. When a person comes in here and says that certain provisions of the bill which they point out will do this and that?

Senator BULKLEY. If you would name the provision certainly I would withdraw the charge of vague generality. That is what I am inviting you to do.

Senator GLASS. Yesterday perhaps you heard an experienced and apparently very intelligent banker, speaking for the whole banking association of his State, say that the requirements of the liquidation corporation would exact a contribution of \$350,000 from his bank, whereas the actual computation showed that the contribution would only be \$87,500.

Mr. PAYNE. I did not hear that statement. I was not here all the time.

Senator BULKLEY. I had a further purpose in asking you that question, because I think there is some language in this bill which certain bankers have misinterpreted, and I think that their misinterpretation is pretty readily understandable. Two or three bankers have criticized one part of this bill and have promptly withdrawn the criticism when it was explained to them what the

section really meant; and I was wondering if you were one of those that had been deceived in that way.

Mr. PAYNE. What provision is that?

Senator GLASS. The provision about "the purchasing and selling hereafter."

Senator TOWNSEND. Section 15.

Senator BULKLEY. Concerning the amount of securities which banks may purchase and hold for their own account.

Mr. PAYNE. I am frank to say that, on my first reading, I think your language seems to be rather vague, but I did not interpret it the way I heard it in some—

Senator BULKLEY. You do not think there is anything to be alarmed about that, do you?

Mr. PAYNE. No; I do not.

Senator BULKLEY. It has generally been agreed that it is not alarming when they understand what it means.

Mr. PAYNE. Yes. Of course, I would rather see the bill become a law with a little more specific explanation about that.

Senator BULKLEY. I quite agree with you that the language would have to be clarified.

Senator GLASS. Yes. We have repeatedly stated to witnesses we are glad to clarify any of the language there that seems to be misunderstood; but that does not seem to make any impression on succeeding witnesses. They devote themselves to identical criticisms.

Senator BULKLEY. Some of them have not heard the other witnesses.

Mr. PAYNE. I assume that is largely the purpose of these hearings, to bring out those defects, so we may explain what seems to be a defect is not really a defect.

Senator GLASS. Most of them stick to the curriculum.

The CHAIRMAN. Have you any further statement?

Mr. PAYNE. Yes. There are one or two other things I would like to say if I do not trespass too much on your time.

On the question of the branch bank business: Many of our country banks have long given their community satisfactory service under the unit banking system and view with some apprehension a further extension of chain and branch banking. My own opinion is that this system will grow as, if, and when it suits the business needs. It is a slow and evolutionary growth, and its final form will come through the trial and error system. Whatever legislation is enacted will not be perfect; there will be defects in it, and during that time of experimentation it will be costly to the banking system, but I think it has got to come.

Senator GLASS. What has got to come?

Mr. PAYNE. Experiments as to what is the ultimate form of our banking system. But it seems to me that this is not the time to go through those experiments. If you gentlemen feel at all the way I feel about the serious situation we are in now, it seems to me you can agree with me that anything in the nature of experimental legislation looking to a change or to new forms of the machinery of business should not be undertaken at the present time.

Senator GLASS. But we have had witness after witness to tell us that we not only should have branch banking but that we should go into States regardless of State laws.

Mr. PAYNE. That may be so, Senator. I do not think any of us can predict what the ultimate form is going to evolve out of this system. I think there are going to be changes as there are in practically every other form of business activity, retailing and other things, but it seems to me this is not the time to begin those experiments.

Senator GLASS. Do you favor general banking or group banking?

Mr. PAYNE. Do I favor it?

Senator GLASS. Yes.

Mr. PAYNE. Frankly, I do not know what the solution is. We have grown up under a unit system and we like it. I do not think it is going to continue. Of course, it is not now the only system. We are going through an evolution, and what the ultimate outcome is I do not know. I wish I did.

Senator BROOKHART. You are not familiar with cooperative banking?

Mr. PAYNE. Only by some reading on the subject. That is a very interesting experimentation. It might possibly be the ultimate solution of the thing.

Senator BROOKHART. It is not an experiment any more in the countries that have tried it. It is the oldest and best established system, the cooperative.

Mr. PAYNE. Of course, opinions may differ on that. I think it is going through some experimentation yet. I may be wrong.

Senator BROOKHART. That is in countries that have not tried it or are just beginning.

Mr. PAYNE. I do not think any form of business machinery is static.

Senator FLETCHER. Do you mean to say that the present banking laws as they stand now are satisfactory and ought to be let alone, or do you feel that—

Mr. PAYNE. Not entirely, Senator.

Senator FLETCHER. Or do you think there ought to be some changes and improvements on the present banking laws?

Mr. PAYNE. I think we can always improve our machinery.

Senator FLETCHER. Then why not do it?

Mr. PAYNE. But I do not think at a time when our Nation is so sick—and it has affected a great many towns, and whether a certain town is going to have a bank failure is a serious question from week to week—I do not think that is the time to do it. That is the one time when we should have a rest. That is my general attitude.

Now, there are just one or two specific provisions here—

Senator GLASS. Many of them have gone to their eternal rest, have they not?

Mr. PAYNE. I know they have, and I want to save some others from going through if I can.

There are two or three provisions of the bill which I believe are particularly disturbing to banks in agricultural communities. I would like to call to your attention section 11, penalizing the use of other than eligible paper in borrowing from the Federal reserve banks. Many country banks in small communities often have little eligible paper (in spite of the figures you have on the whole amount) at the time they need to borrow in order to make needed loans to their neighbors. These loans are based largely, not on tangible

security, but on the intimate knowledge of the banker of the character, habits, and earning ability of the borrower. We loan a great many farmers on our knowledge of the fact that for 50 years, perhaps, he has on the whole successfully conducted his business. It does not create eligible paper, and in the small community we get very little eligible paper, comparatively speaking, to what we used to get from our merchants and our small manufacturers.

Senator GLASS. Do you make farmers' loans for 15 days?

Mr. PAYNE. Loans to farmers, do you mean?

Senator GLASS. For 15 days; yes.

Mr. PAYNE. Oh, no.

Senator GLASS. What is it you are talking about? What particular provision do you say you are talking about? Section 11 of the bill?

Mr. PAYNE. Section 11; yes.

Senator GLASS. How does that interfere with the loans to farmers?

Mr. PAYNE. Well, I say if we are penalized for using something besides eligible paper to get money from the Federal reserve bank when we need it—

Senator GLASS. On 15-day paper?

Mr. PAYNE. Yes.

Senator GLASS. You make loans to farmers for 15 days, do you?

Mr. PAYNE. Oh, no.

Senator GLASS. I do not exactly understand.

Mr. PAYNE. We borrow from time to time when we need it, in the peak loads.

Senator BULKLEY. How often do you use this facility of borrowing on the 15-day note?

Mr. PAYNE. I should say we are in and out of the bank perhaps 20 per cent of the year. We borrow for a few days, build up a reserve, and carry the peak and are out again.

Senator BULKLEY. Most of it you carry?

Mr. PAYNE. Practically all. We very seldom rediscount. We carry \$1,000,000 of Government securities.

Senator BULKLEY. You find it the more convenient way of borrowing? Even if you have the eligible paper you are likely to use the Government securities?

Mr. PAYNE. Yes. It is very seldom we borrow by rediscounting.

Senator BULKLEY. You find it more convenient to complete the transaction?

Mr. PAYNE. It seems to me a waste of time in the Federal reserve bank. We send down our note and that is all there is to it. There is no question of getting together a lot of statements and scrutinizing notes, perhaps throwing out some and substituting others. We find it much more convenient.

Senator BULKLEY. You are speaking for your own bank?

Mr. PAYNE. Yes.

Senator BULKLEY. Do you think that is true generally of some other banks?

Mr. PAYNE. I do not know, of course, the intimate practices of a great many of the other banks, but I know some of the banks of our character that have the same experience. Just how universal it is I could not tell you.

Section 13 increases the reserves on time deposits in country banks to 7 per cent. Most of the country banks, especially in towns where there are no savings banks, have a large percentage of their deposits on time. These are the banks, in my opinion, that at this time need every dollar of profits they can legitimately earn, and therefore I think that this is no time to bring that in, if it is desirable. Personally I can not see any desirability of doing that. I do not think the Federal reserve banks need those reserves, and it seems to me it is just taxing, cutting down the earnings of our banks. I can not see any particular reason for doing it.

Senator BULKLEY. It is generally agreed by expert opinion that reserves are not too low.

Mr. PAYNE. No. I do not think they are too low.

Senator BULKLEY. We have plenty of testimony on that.

Mr. PAYNE. You do think so? Our own experience is that when the reserve limit was cut down before it changed our cash reserves very little. In other words, the lower the amount we had in the reserve bank, the more we kept in our own till or with our New York correspondent. We know from time to time about how much cash reserves we need and we keep them.

One other proposition—

The CHAIRMAN. Your time expired quite a while ago. We have one more witness to hear before noon, so we might as well close it up.

Senator BULKLEY. I think it is largely my fault.

Mr. PAYNE. Section 14 provides for segregation of time deposits and limits their investment to real estate loans and securities legal for savings banks. In my section of the country such a limitation would deprive many communities, I believe, of the opportunity to borrow from the bank the funds to which they are legitimately entitled.

Senator TOWNSEND. What are the total deposits of your bank?

Mr. PAYNE. About \$7,000,000 now.

Senator TOWNSEND. How are they divided?

Mr. PAYNE. A little more than \$4,000,000 in time deposits and the rest in demand deposits. We have two good savings banks in our town. They have a large proportion of savings accounts in some of our surroundings banks, and they do all the savings business there. A very large proportion of their deposits are savings deposits. I do not know how they are going to finance their little community and the surrounding country unless they can use those funds for it. They are the funds gathered into the community for the purpose of the use of the community, and I believe they ought to be available for loaning.

That is all I have, and I thank you very much, sir.

Senator WAGNER. I would like to say if there is anything further you want to communicate to the committee, will you send it to me?

Mr. PAYNE. Thank you, Senator. I shall be glad to send it to you.

The CHAIRMAN. Mr. Wakefield.

STATEMENT OF L. E. WAKEFIELD, PRESIDENT OF THE FIRST NATIONAL BANK OF MINNEAPOLIS, MINN.

Mr. WAKEFIELD. Mr. Chairman and gentlemen: The First National Bank of Minneapolis, of which I am president, is a member

of a group system operating in the ninth Federal reserve district and principally in the four States of Minnesota, North and South Dakota, and Montana.

I shall confine my remarks to the effect of this bill in its present form on group banking as it exists in the Northwest. I believe that the purpose of the bill is constructive and contains great possibilities for good, but after careful study we in the Northwest are convinced that it should be altered in several particulars to avoid a harmful result which outweighs helpful features.

By way of introduction I would like to state in a word what group banking, with us, means. Most of the banks of our group are national banks. The stock of these banks is owned by a holding company and for the most part was acquired by exchanging the stock of the holding company for the stock of the banks, so that each original stockholder in an individual bank continues to be a stockholder but with his stock interests spread over a number of banks instead of being confined to one single bank. The result of this exchange amounts, in practical effect, to the creation of a partnership, in which all the partners obtain the benefit of diversity of assets, increased efficiency of management, and economy through standardization of banking methods. Inasmuch as the two cities of Minneapolis and St. Paul predominate enormously in population over the rest of our territory, which is largely rural, this partnership is in reality a partnership existing between the cities and the country.

Up to the present time the partnership has turned out to be a poor one for the cities and a correspondingly advantageous one for the country, because the extreme depression in agriculture and agricultural values, resulting in heavy losses to the country banks and a great increase in their frozen assets, has not only made it impossible for these banks to produce their share of the earnings of the partnership, but has made it necessary for the holding companies to supply them with large sums of money to restore their impaired capital and reserves and keep them in a sound and safe condition. However expensive this has been for the cities, it has in fact proved of inestimable value to the district as a whole. We have had numerous failures of small independent banks, but we have had no big bank failures. In spite of the disappearance of farm land values, in spite of drastic reductions in the price of farm products, cattle, etc., and in spite of drought and grasshoppers, we have succeeded in maintaining a sound banking structure for the people of our section, and this success can only be attributed to the strength which is inherent in the group system of banking.

We did not, as in the case of our friends in Michigan, remain within the borders of one State, for the simple reason that, with the possible exception of Minnesota, there is no one State in our territory which of itself affords sufficient diversity of resources to make group banking, thus limited, either profitable or safe. The development of the past two years makes it clear that any group banking system which had attempted to operate in Montana alone or in North Dakota alone or in South Dakota alone would have had the most disastrous experience and would probably have involved any one of those states in a complete collapse of its banking structure.

Our task is by no means completed. We are willing to accept the responsibility for completing it and hope to do so without ask-

ing any financial assistance from the Reconstruction Finance Corporation, the National Credit Corporation, or any other agency. We only ask that we be not hampered or hindered by the enactment of legislation which would make our task any more onerous than it already is.

Naturally that portion of this bill which is of paramount and absolutely vital importance to us is section 20, which prescribes that group bank holding companies shall maintain certain reserves in assets other than bank stocks for the purpose of protecting any future stockholders' liability. The enactment of this section as written would completely put us out of business, or at least force us out of the Federal reserve system. This is not a threat; it is a plain statement of fact. We do not want to abandon the Federal reserve system, but we are physically unable to comply with these requirements. The assets which would have enabled us to maintain these required reserves have been depleted by contributions to our country banks for the purpose of restoring their capital and reserves. Even if this were not so, we think the reserve requirements are altogether too severe and that they are particularly unwise in that they require the holding company to maintain them in a frozen condition and only permits their use after a bank has failed rather than allowing them to be used to prevent such failure.

I understand that an amendment is before the committee which reduces these reserve requirements and makes them available by way of prevention before failure as well as a cure afterwards. If this amendment is adopted, it will remove our objections to section 20.

The other provision of the section, requiring reports and examinations of the holding company and its affiliates, have our hearty approval and support.

The next subject of great interest to us as group bankers, and of even greater importance to the communities we serve, is the matter of branch banking, section 21 of the bill. As this section is now drawn, with the limits as to State law included, it accomplishes nothing so far as the Northwest is concerned. If this limitation were removed, it is almost impossible to exaggerate what it would accomplish in our territory. I recognize that in advocating state-wide branch banking at this time, I am departing from opinions I expressed in my testimony before the subcommittee a year ago. I admit that frankly. We have learned by our experience of the last three years how much more effective branch banking would be than group banking. I do not think that a year ago the people in the country districts were ready to accept branch banking, but this sentiment has undergone a great change, and I am certain that the majority of these people are not only no longer opposed to branch banking but anxiously hoping that it will be accomplished with least possible delay.

Aside from the correction of faults and abuses which have developed in the banking business during the last few years, it is essential that any banking legislation should be directed toward relieving the emergency which exists at present in the banks of the country, by preservation of the deposits in existing banks, the restoration of confidence by the prevention of further bank failures, and the estab-

lishment of a sound banking structure as the prime requisite to revival of general business.

At this time there are a large number of banks open and operating where the capital and surplus have been impaired through depreciation in the value of securities held and losses on loans caused by the general depression. In addition to this, there are many places which formerly had banking facilities, but which are not now being served by any bank. I believe that the only thing that can even partially save or correct this situation is a law which will authorize state-wide branch banking by national banks immediately and without waiting for the State legislatures to meet. I make this statement for the following reasons:

At the present time it is not possible to raise capital for the purpose of establishing small banks in communities which are not now served.

The public authorities, the comptroller's office, and the various superintendents of banks, in their anxiety to hold our banking system intact so far as possible, are at present carrying on with a large number of banks whose capital and surplus have been impaired by both depreciation and losses. They are doing this in the hope that banking legislation will provide some means whereby the deposits in these banks can be rescued and taken over into sound banking institutions and be preserved as live deposits instead of turned into the obligations of a closed bank. There are a large number of these institutions which could furnish a sufficient amount of sound assets so that their deposit liabilities could be assumed by another bank as a branch office. The local stockholder has, to a large extent, suffered business reverses; he has paid in additional capital to his bank in the past and is no longer able to supply the funds necessary for recapitalization at this time.

For these reasons it seems to me imperative that if there is any desire on the part of Congress to preserve the greatest amount of our present bank deposits, Congress should recognize this situation and provide a means immediately which will make this preservation possible.

The suggestion is made that Congress is loath to legislate arbitrarily in this matter, preferring to leave the ultimate decision to the legislatures of the various States. To me this is inconsistent with the principles underlying the national banking system. This system was established by Congress without regard to State law, and Congress has jealously retained all rights and supervision over it, so that any amendment to the national bank act could not be legitimately considered as an interference with the sovereign rights of any State. Furthermore, if the matter is left to the States, and national banks are granted the same branch banking privileges as are granted to State banks, we shall have the national banks of the country operating under 48 different branch banking laws.

Just as a matter of interest I would like to refer to the fact that the Reconstruction Finance Corporation is experiencing the greatest difficulty in confusion on account of its having to adopt itself to these various State laws—48 different systems, each one having its own regulations and of a very peculiar nature; and the provision authorizing national banks to operate branch banks, as provided by State law, would simply mean the bringing of that same

confusion of regulation and privilege into the national banking system, which now prevails among the 48 States, and it seems to me to be a very undesirable thing to do.

The advantage of having the entire system operating under one standard law is too obvious for argument. Aside from all this, however, the controlling factor is time. If this matter is delayed for the time necessary to secure State legislative action, the various banking departments will not be able to put off taking the steps necessary to remedy the present condition, which can only result in a great increase in the number of closed institutions. A year's delay would be fatal. Every bank which closes between now and next year represents a local tragedy. Each one which might have been prevented by branch banking at this time will forever stand as a reproach to the legislative body that might have saved it by the exercise of political courage when it was most needed.

The CHAIRMAN. Would you be willing to take over all the banks out there if you could?

Mr. WAKEFIELD. That would have to be done under regulations that would permit it.

The CHAIRMAN. Would you take over the solvent and the insolvent also?

Mr. WAKEFIELD. As far as it would make possible negotiations. Not all of them by any means.

The CHAIRMAN. I suspect, when this would come as a remedy, you would find three classes of banks: First, those you could not buy; second, those you would not buy, and the third, the ones you would dicker for.

Mr. WAKEFIELD. I think it is the most favorable time, if there is ever going to be a time, to permit branch banking for this reason—

The CHAIRMAN. I do not care to go into my argument on that Mr. Wakefield, but I thought your statement was too broad, holding out the hope that branch banking will save the situation, the trouble of ours which has an underlying cause. If you advocated a better price for the farm products up there, the banking situation would respond to something of that kind. Our trouble is agricultural, rather than banking. That is my view.

Mr. WAKEFIELD. Yes; you are correct. In the meantime there is a large portion of those existing banks which could be rescued.

The CHAIRMAN. You know how it is. It is like salvation. Some want to be rescued and some do not want to be rescued. You can only buy those that will sell to you, and you would only buy those that you thought were sound.

Mr. WAKEFIELD. You certainly would not step in and assume a large loss for the sake of protecting some deposits.

The CHAIRMAN. That is exactly so.

Mr. WAKEFIELD. Although we have in the past assumed our share of it.

The CHAIRMAN. You heard Mr. Decker's statement down at the Willard Hotel a month ago, did you not?

Mr. WAKEFIELD. Yes. I remember that.

The CHAIRMAN. He said the small banks have got to go.

Mr. WAKEFIELD. I do not agree with the statement that small banks have got to go, but a great many of them have gone.

The CHAIRMAN. And so have some of the big ones, and the big ones have been yelping around here all winter for help. We passed a \$2,000,000,000 finance corporation bill mainly to help the big banks.

Senator GLASS. One of them alone got \$40,000,000.

The CHAIRMAN. Yes. So I can not see the point that there is strength in bulk only.

Mr. WAKEFIELD. There is not.

The CHAIRMAN. No.

Mr. WAKEFIELD. No one has intimated it. I have not intended to intimate it.

The CHAIRMAN. I did not mean to interrupt you so long.

Mr. WAKEFIELD. I am only seeking to point out the only spot that I know of which we know could be created, which would make possible at this time the rescue and maintenance of a substantial portion of now live deposits and continuing them in that shape.

There is probably no man on this committee who does not believe that branch banking in some form, and at least state-wide, is inevitable sooner or later. If so, no time could be selected when it would do more good than at present. It has been suggested that group banks be permitted to convert their present units into branches, restricted by State boundaries. If for political reasons it is impossible to obtain branch banking at this time, the alternative would, of course, be welcome. It would be of enormous help to us in carrying out the difficult work we are now engaged in, but there is no denying the fact that it would not supply the needs of the rural communities which I have mentioned. It would not enable us to prevent further failures of small banks, nor would it enable us to furnish banking service to communities which now have none.

We would respectfully urge that section 21 be amended by striking out from page 45, lines 21 and 22, the clause: "If such establishment and operation are at the time permitted to State banks by the law of the State in question."

The third subject matter of this bill of great importance to us is section 13, which increases the reserve requirements for national banks. This provision would crucify the country banks in the Northwestern States. The principal disease which those banks are suffering from is lack of earnings, hence the thing which would hit them the hardest is anything which would further reduce their earning power. Loans from the National Credit Corporation or the Reconstruction Finance Corporation can not cure this evil. They are only palliatives. Those loans must be repaid by the borrowing banks.

I would like to show the committee what this section would do to the four Northwest States of Montana, North, and South Dakota, and Minnesota. Based on the call statement for December 31, 1931, the total reserve requirements when the 5-year plan is fully in effect would be increased as follows: Montana, \$1,370,000; North Dakota, \$1,300,000; South Dakota, \$972,000; Minnesota (rural), \$5,200,00; Minnesota (Twin Cities), \$9,000,000; total, \$17,842,000.

Assuming an average earning power of 5 per cent this means a loss of income to the national banks of these States in the annual sum of \$392,000. This would perhaps not be considered a large amount of money in any of the large eastern States, but it is a very large amount for us in the Northwest. Under present conditions and under conditions as they will probably continue for a number

of years, the banking structure of the Northwest can not afford this loss.

Senator GLASS. How many banks in the Northwest failed before the reduction of the reserve requirement? How many of them were crucified?

Mr. WAKEFIELD. Of course, those conditions are past and we are operating under conditions prevailing to-day, where losses are great and earnings are hard to make.

Senator GLASS. You do not agree with Mr. Jefferson, then, that experience is worth anything?

Mr. WAKEFIELD. I have no knowledge of any bank having failed on account of not having enough reserve.

Senator GLASS. But they were not crucified before we reduced the reserve from 7 per cent to 3 per cent, were they?

Mr. WAKEFIELD. No; but they were then operating on a different basis of relationship to their customers, and if you now change it so that their earnings are reduced, they have got to work through a period of readjusting their relationships and regulating incomes in some way.

Senator GLASS. In what way are the relationships different now than the relationships formerly?

Mr. WAKEFIELD. They have extended the services and changed the rates on loans, and they are operating on a different relationship. Those things are bound to come.

Senator GLASS. I would like to get hold of a bank that has changed its loans, that is, if it has reduced its discount rate.

Mr. WAKEFIELD. You ought to go up in the Northwest, where we have real competition.

I understand that it has been suggested that the so-called "activity reserve" be substituted as an alternative for this section of this bill. The chief difficulty with the activity method is that in agricultural sections it increases the reserve requirements during the crop-moving periods at just the time when the banks' resources are most needed by their customers. However, there is no question but that the activity method would be far more acceptable to us than the section as it is now written. It would increase our reserves substantially but nowhere near as much as under this bill.

So far as I know, there is no necessity for increasing the total reserve requirements of national banks at the present time, either as a measure of safety or for supplying additional funds to the Federal reserve. It seems that this section as written was inspired by the misbehavior and abuse of some banks in so juggling their deposit accounts as to get the benefit of the lower reserve rate on deposits which for all practical purposes were, in fact, demand deposits.

Senator GLASS. You know, our information was—and, I think, very definite and authentic—that that was being largely done by the banking community.

Mr. WAKEFIELD. It is an experience that I know nothing about.

Senator GLASS. And the increase in the shift from savings deposits to time deposits would indicate that that was true.

Mr. WAKEFIELD. Of course there has been a very large increase in time deposits during the last few years, due to the unemployment of large corporate funds and the fact that they are carrying certificates instead of borrowing money. That is true to-day.

Senator GLASS. We were told a good deal of it was due to the fact that banks shift from demand deposits to time deposits in order to avail themselves of the 3 per cent requirement.

Mr. WAKEFIELD. The difficulty there, Senator Glass, is that a shift in savings banks costs too much money. In our case we could not afford to shift but very few demand deposits to time deposits. The savings in the reserve would have been eaten up a couple of times by the increased rate of interest. So it would not work with us at all.

Senator GLASS. It may not have worked with you, but it seems to have worked with some of them.

Senator FLETCHER. What interest do you pay?

Mr. WAKEFIELD. Three per cent on time deposits.

Senator FLETCHER. How much on the demand?

Mr. WAKEFIELD. One per cent of the demand deposits. I imagine it would put us all out of kilter to do that. We could not.

If this is so, it would seem more appropriate to enact legislation which would prevent the continuance of these abuses rather than penalize all of the banks of the country, including the innocent with the guilty. However, if this is not practical, and it is felt that the temptation to juggle accounts should be eliminated by abolishing all distinction between the two classes of deposits and fixing one rate for both, then such rate ought to be fixed at a point between the present rate on demand deposits and the present rate on time deposits, so that the total reserves required shall not in the aggregate be any greater than they now are. For example, again based on the call statement for December 31, 1931, this method would result in the following reserve requirements: Central reserve cities, 11.6 per cent; reserve cities, 6.7 per cent; nonreserve cities, 4.7 per cent.

These figures are only based on one call rather than a study of an average over a period of time, and hence are used only as an illustration. The principle I am suggesting, however, would entirely remove the criticism made by Senator Glass, would not in the aggregate place a greater burden on the banks than they are now under, would remove all controversies as to when a time deposit is not a time deposit, and would greatly simplify the administration of the law.

Senator GLASS. Why do you say the criticism made by Senator Glass?

Mr. WAKEFIELD. Perhaps I am wrong in that, Senator Glass. It is your committee that has made it.

Senator GLASS. Well, it is based upon criticism made at the very prolonged and searching hearings that we had last year.

Mr. WAKEFIELD. I am willing to amend it to say it is criticism which developed in the hearings.

Senator GLASS. If it is being done I am unhesitatingly criticizing it as a species of dishonesty. It ought to be penalized. Go ahead.

Mr. WAKEFIELD. There is one other provision of the bill to which we object strongly. That is section 14. I can see no possible good that would be accomplished by this section, but on the contrary a great deal of harm. It would be ruinous to the country districts. In Montana and South Dakota savings deposits are 50 per cent of the total in the national banks. In North Dakota they are 60 per

cent. In rural Minnesota they are in excess of 60 per cent. Even in the city of St. Paul they are more than 50 per cent and in Minneapolis more than 40 per cent. In other words, more than half the deposits available for the business needs of the community would be withdrawn under this section. Instead of encouraging the making of real estate loans, it would practically terminate them altogether. The loss of earnings which would result in investing all this money in Government bonds, municipals, and the other low-rate types of securities permitted by State law, would be disastrous. The preference created in favor of time deposits in event of bank failure would further stimulate the increase of time deposits even beyond their present high proportions.

Senator GLASS. What becomes of State banks under the requirements of State law as to the investment of time deposits?

Mr. WAKEFIELD. Only savings banks in Minnesota. The State banks have the same requirements that national banks do as to investment. There is no segregation in Minnesota.

Senator FLETCHER. What change is it you are afraid of?

Mr. WAKEFIELD. Demanding segregated time deposits and stipulating an arbitrary class of securities in which they shall be invested.

Senator GLASS. Your State laws do not do that, do they?

Mr. WAKEFIELD. No, they do not, a bank down in Austin has 75 per cent of their deposits in time deposits, and yet there is a considerable demand there for good loans. It is quite a town, a town of 12,000 people. It would result in our having to withdraw our loans from the community down there—the people that are doing business, the business people in town, and the farmers that come in—and comply with the legal type of investment, just as a savings bank. We have a savings bank law in Minnesota, and this would place us under the savings bank law, which would mean that we would have to buy municipals and certain specified types of securities, all of which are of very high grade and bear a low rate of interest.

Senator GLASS. That is very much better than many that have been bought.

Mr. WAKEFIELD. The peculiar thing about that, Senator Glass, is that it is the very type of securities that we are not interested in getting into at the moment.

Senator GLASS. It is better than these \$12,000,000,000 of farm loans that have been unloaded on the banks of the country, at any rate.

Mr. WAKEFIELD. I think that would be as a class very true; yes.

Senator BULKLEY. Do you refer to this provision restricting investment to property and securities in which savings banks may invest under the law of the State? Is that what you were referring to?

Mr. WAKEFIELD. Yes. It is that definite segregation of your savings deposits. For instance, there is another thing about that. You take in the city of Minneapolis to-day, you know that the grain business is using no money because there is no business. Our grain people are all of them long on money and they are carrying a lot of money on time deposits. That increases our time deposits very materially. That would mean that we would have to try to buy savings bank securities for those deposits. We could not use them in any other way, knowing that in 9 months, when a crop starts, we do not know what day or what period, in 30, 60, 90, or 120 days, or

a year, those funds are going to be out, and there you have that money temporarily that you know is time deposits but you can not use it.

Senator GLASS. Can you recover your funds from investments in real estate any more readily than you can from these?

Mr. WAKEFIELD. No.

Senator BULKLEY. You are not objecting to the limitation on real estate?

Mr. WAKEFIELD. No. I do not care about that.

Senator BULKLEY. You are objecting to the limitation as to the use of other funds?

Mr. WAKEFIELD. Yes. I am objecting to the attempt to segregate and put into one class a private, arbitrary type of investment for all time deposits.

Senator BULKLEY. I do not quite understand your use of the term "segregate." What additional segregation is there?

Mr. WAKEFIELD. That would mean we would have to run our books on the basis of our investments. We would have to set out our total savings deposits and we would have to use those deposits with an entirely different class of investment than the general business of the bank. That is, if some man came in and wanted to borrow half a million dollars on wheat receipts in the elevator and we had nothing but time money available at the time, we would have to go to the Federal reserve bank. Even though we had funds to loan we would have to go and borrow the money to loan to that fellow. It is a condition that just makes almost an impossible bank transaction, and it penalizes the bank very materially.

The CHAIRMAN. Would it be apt to meet the situation in your city bank as it would in country banks?

Mr. WAKEFIELD. I think we would meet it much more in the city bank than we can in the country, because they just have not any place to go. It would be very difficult when it comes to the country bank.

The CHAIRMAN. In other words, their main difficulty from this provision would come with the smaller banks?

Mr. WAKEFIELD. Yes, it would.

Senator BULKLEY. Your thought is you ought not to be precluded from making commercial loans out of the time deposits?

Mr. WAKEFIELD. That is exactly it. My thought is it is all right to specify what percentages you can have in real-estate loans. I think it is very desirable that it be done, but any attempt to fix an arbitrary regulation as to how the balance of those funds should be used from time deposits creates a hardship which I think will penalize the public doing business with the bank very severely.

Senator FLETCHER. What precise language compels that?

Mr. WAKEFIELD. It is in section 14.

Senator BULKLEY. Page 33, line 20.

Senator FLETCHER (reading). "Every such bank may apply the moneys deposited therein as time deposits——"

Mr. WAKEFIELD. Then it tells you just how they can.

Senator BULKLEY (reading): "To the loans herein authorized——." That refers to real-estate loans. Then it goes on further: "and the balance of such time deposits shall be invested in property and securities in which savings banks may invest——"

Mr. WAKEFIELD. That is the place from which almost the bulk of your objection to this thing in the country will originate. It is very serious with them.

I have a telegram right here which came from the secretary of the Minnesota Bankers' Association. May I read it? He asked me to. He says [reading]:

The rural independent and group bankers unanimously agree that provision in the Glass bill segregating deposits is very detrimental to rural communities. Rural deposits mostly time money. The Glass bill prevents investing funds locally. Agricultural sections should not be restrained from their investments. Many rural banks prove that local conservative loans are even superior to savings-bank loans, therefore offers no further protection to savings depositors. To comply with this provision within the time limit would close most of our national banks.

They all join in the feeling that they could not convert their present loans, get them out, and get into this other type within any reasonable time and do it safely.

It says further [reading]:

Increased reserve requirements would reduce earnings and result in weaker banks suffering. Our independent rural national banks would be forced into the State system because of the above and other provisions. Rural bankers ask you to present their case before the bank committees in Minnesota delegation in Congress.

GEORGE SUSAN,
Secretary Minnesota Bankers' Association.

Senator FLETCHER. Do you have savings bank laws in your State?

Mr. WAKEFIELD. Yes.

Senator FLETCHER. This reads:

where there is no such law relating to investments by savings banks, in such property and securities as may be specified by the Comptroller of the Currency.

Mr. WAKEFIELD. They would be obliged in those cases where there are no savings bank laws to set up, that is, the natural liberty would be to set up a list of securities that do comply with the general savings bank requirement. In view of the fact that it has been said definitely to meet the savings bank requirements of the various States that have them—and most of them do—I do not think that the comptroller would feel that he had any liberty to set up a different type of security for those States not having it.

Senator BULKLEY. I think you are justified in that. It says, "property and securities," and therefore would not permit commercial or agricultural loans.

Mr. WAKEFIELD. No.

Senator BULKLEY. I think you are right.

Mr. WAKEFIELD. You see, it classifies them and limits it completely to those legal investments, which is a serious matter.

The banking system of the country can not be strengthened by reducing the banks' normal earning power. Such measures have just the opposite effect. The condition in the Northwest is such that very properly we might have asked Congress for legislation which would increase the earning power of banks, particularly of country banks. We have not done that but do ask that this earning power be not decreased any lower than it is.

The unfortunate feature of both section 13 and section 14 is that they fall with the greatest force upon the banks in the agricultural communities, who are least able to withstand the blow. In my

opinion, the bill should be amended by striking out section 14 altogether.

There are two other provisions which I would like to mention.

Section 10 requires national banks to contribute a substantial amount of capital to the Federal liquidating corporation, in whose management, however, they are given no voice. This seems a particular hardship on the group of banks of the Northwest.

Senator GLASS. Why do you think they are given no vote?

Mr. WAKEFIELD. They have no vote.

Senator GLASS. Well, the banks do have a vote.

Mr. WAKEFIELD. How?

Senator GLASS. They elect six out of every nine directors of the Federal Reserve.

Mr. WAKEFIELD. No; you have disfranchised us from electing any directors in our district.

Senator GLASS. We ought to disfranchise you if you are operating under a system that enables a holding company to control the entire Federal reserve banking system of the zone.

Mr. WAKEFIELD. We do not want to do that.

Senator GLASS. Your remark there was not directed to your particular system of group banking; it was directed to the whole proposition. The member banks select six of the nine directors of the Federal reserve bank, and therefore the matter is in their control. If the manager of this liquidating corporation selected by the Minneapolis bank is not satisfactory to the member banks of that zone they can select somebody else; so that altogether it is in the hands of the member banks to manage.

Mr. WAKEFIELD. That is, the foreign and open market committee that became the directors of the liquidation corporation?

Senator GLASS. Yes.

Mr. WAKEFIELD. We feel that we would have some control over who those people were.

Senator GLASS. You would have complete control.

Senator BULKLEY. The banks would.

Mr. WAKEFIELD. Your other question about the voting of group banks is an entirely different question. I did not intend to inject that at this point because I was thinking the same as Senator Glass was.

Senator BULKLEY. I think if you were not injecting that, you did not state it correctly at all.

Mr. WAKEFIELD. I wonder whether that control, though, is close enough so that we could have any effect upon the action of the liquidating corporation in what they did or what they decided to do with our money after they got it.

Senator GLASS. Well, the member banks select the members of the liquidating corporation from the respective Federal reserve districts.

Mr. WAKEFIELD. But there is a combined purpose in the selection. He is the open-market committee man and, incidentally, a director of the liquidating corporation. Now, I can say the thing that puzzled me is—

Senator GLASS. The member banks are the only people who profit by the liquidating corporation except that the depositors in failed banks get the money sooner than they otherwise would do. But

in the distribution of profits you are the only people that really get the profit.

Mr. WAKEFIELD. I was wondering how they are going to get profits.

Senator GLASS. Well, in our conception they would get profits. The corporation would make money and the member banks would get 30 per cent of it.

Mr. WAKEFIELD. The fear that I have in connection with that is that without some direct means of the banks being represented and controlling its management, after having put up the money, they subject themselves to the extreme possibility of loss due to attempts to regulate things and liquidate things that can not be liquidated.

Senator GLASS. You could not have individual banks represented on that committee?

Mr. WAKEFIELD. No.

Senator GLASS. There would be 7,000 members of the committee if we went to them all.

Mr. WAKEFIELD. This seems a particular hardship on the group banks of the Northwest, because we have already drained our resources to clean up banks which would otherwise be candidates for the benefits of this very section, and hence we have in effect already contributed many times over our share of the burden. In order to accomplish this we have cut our salaries from the top down, and in spite of the possible effect upon 18,000 stockholders we have cut our dividend in two. We have also subscribed to the National Credit Corporation. Having made these sacrifices which will save the Federal liquidating corporation many times the amount of our subscription, it seems to us unfair that we should be now compelled to cripple ourselves further by coming to the assistance of other banks when we have all we can do to take care of our own.

Senator BROOKHART. On that proposition: Is it not true the failures of those very banks injure your banks? Will it not be a benefit to your bank if other funds can be distributed earlier?

Mr. WAKEFIELD. It would be, Senator Brookhart. We have tried to do this in a way. The President sent out a letter some months ago suggesting that one of the most favorable things which could occur would be some provision by the going banks in the community for making loans on or liquidating the assets of the closed banks. We took that in good faith, at the request of the Federal reserve bank in our district, and we got together with the State Department and with the Comptroller's office and worked out with the lawyers a legal scheme of doing that, which was quite a complicated affair, and then we went into the country where banks had closed and tried to find a chance to use it, and the real facts are that the bank that has closed as a general rule has drained itself down of every possible liquid thing it has until when it closes there really is not anything left there to go on.

Senator BROOKHART. But there are some of those present assets that are going to and will come around. They will be made liquid by those processes.

Mr. WAKEFIELD. You would find a good many of those put up as collateral for loans that they had already secured.

Senator BROOKHART. You think, then, it can be done?

Mr. WAKEFIELD. I do not think it will be nearly as effective as I think it might be in October and before the Reconstruction Finance Corporation was formed. I think that to-day—and I am only expressing my opinion from what I know of closed banks—that on that particular factor it is over emphasized as to what its benefits would be.

Senator BROOKHART. Do you think the Reconstruction Finance Corporation is doing any good by liquidating the closed banks?

Mr. WAKEFIELD. It is only recently that they have started making loans to closed banks, and I would be very curious to see how far they can go in it because of these difficulties that exist in finding anything to really loan on; but the Reconstruction Finance Corporation has unquestionably done a great deal of good in stopping the closing of banks.

Senator BROOKHART. Yes; but it has done that by lending money, and when the money comes due some of these days you think they will collect on 3-cent hogs and 25-cent corn?

Mr. WAKEFIELD. We are going to have better than 3-cent hogs.

Senator BROOKHART. You are not getting any better yet.

Mr. WAKEFIELD. No, but everything is going to get better.

Senator BROOKHART. The representative of a great organization yesterday said that we were not at the bottom yet and it takes longer to get out of this thing than it does to get in.

Mr. WAKEFIELD. It always takes longer to get out than it takes to get in.

Senator GLASS. And always the time is inopportune to do anything to keep you from getting in.

Mr. WAKEFIELD. That is true. No one wants to let go of anything. I could make you a long speech about that if I had time.

Senator GLASS. We have had them made to us. [Laughter.] I think the most depressing thing that has ever happened in this country is the testimony we have had around this table.

Mr. WAKEFIELD. I am sorry to have been a contributor to that depressing testimony.

Senator GLASS. Only to a very limited extent you have. [Laughter.]

Mr. WAKEFIELD. Just one other matter I wish to mention, and that is the much argued question of security-company affiliates. To whatever extent these affiliates are allowed to continue under this bill, either as now drawn or in its final form, we feel that the law should be universal in its application and that all national banks should enjoy the same privilege, or lack of privilege, as the case may be. There is no possible reason why national banks should be discriminated against simply because they belong to a group system. This bill does discriminate against them in section 20 (e) and this subsection should be eliminated. If, in the last analysis, the committee decides that security-company affiliates should be abolished altogether, we shall make no complaint, but to whatever extent they are permitted to continue to exist, we ask only that our national banks be given the same privilege as the other national banks of the country.

Senator GLASS. If we should have state-wide branch banking you would be in favor of abolishing affiliates, would you not?

Mr. WAKEFIELD. I do not think it could be done, Senator Glass; not within the limit of a good many years.

Senator GLASS. Well, of course we will not close them up instantly. We will give them time to liquidate.

Mr. WAKEFIELD. For instance, we have what we call the Agricultural Credit Corporation, which you may have heard of.

Senator GLASS. I thought you wanted to get rid of your affiliates and make branches of them.

Mr. WAKEFIELD. Yes, but you can not make branches of a concern organized to permit farmers to buy stock and get them on a 5-year payment plan and put them out on their farm. We would have to liquidate that corporation and go out of business. We are willing to do all of that if it is required, but I think it would work a great hardship.

Senator FLETCHER. How many affiliates have you?

Mr. WAKEFIELD. We have about 107 banks.

Senator FLETCHER. In what States?

Mr. WAKEFIELD. Montana, North and South Dakota, and Minnesota. Four in the upper peninsula and two in the ninth district.

Senator FLETCHER. Most of them in Minnesota?

Mr. WAKEFIELD. No. There are about 50 per cent in Montana, North and South Dakota, and northern Michigan.

Senator FLETCHER. You would be willing to transfer them into branches?

Mr. WAKEFIELD. Yes. We could very easily.

Senator FLETCHER. Do all those States allow branch banks?

Mr. WAKEFIELD. None.

Senator FLETCHER. None of them?

Mr. WAKEFIELD. No; we have no branch banking.

As to the advisability or inadvisability of abolishing security company affiliates, I make no argument, but simply the suggestion that the committee would do a greater service to the country by retaining and regulating the security business through the power which Congress has over national banks than by driving that business into less responsible hands over which Congress has no power of regulation.

There are a number of minor errors, or what we conceive to be errors, or phraseology in the bill where the actual language used does not express what we believe to have been the intent of the author. I will prepare a list of items with the suggestions for the appropriate changes and hand it to the chairman.

That is all of my statement, sir.

Senator FLETCHER. That is a very good statement.

The CHAIRMAN. I would like to present for the record a letter by the South Dakota Superintendent of Banks, together with a brief against branch banking, also a letter from Mr. Don W. DeVay, an independent banker of West Port, S. Dak. I would like to have them printed following this reference, if there is no objection on the part of any member of the committee.

(The matter referred to by the chairman is here printed in the record in full, as follows:)

DEPARTMENT OF BANKING AND FINANCE,
Pierre, S. Dak., March 22, 1932.

Senator PETER NORBECK,
United States Senate, Washington, D. C.

DEAR SENATOR: I sincerely appreciate receiving your letter of March 19 with reference to the Glass banking bill. I also received a copy of the bill which you were kind enough to send me.

I have read the bill but I am frank to say that I do not fully understand it. I infer from the bill that no national bank can establish branches unless the parent bank has a paid-up capital of not less than \$500,000. This would preclude any of the present banks in South Dakota, unless their capital is increased, to establish branches. This restriction may be desirable but it would appear to me that if State laws were enacted in harmony with this requirement that the banking business would eventually be controlled by institutions and individuals in the larger places. In my opinion, one of the most objectionable features of this bill is found in section 21 of the bill which provides that even though our State did not enact laws permitting State banks to have branches, a banking institution in an adjacent State, but not beyond a distance of 50 miles from the seat of the parent bank, could establish branches. Just as an illustration, Sioux City, because of its location and prominence, would be an ideal location for a parent bank to be located and reach into southeastern South Dakota with branches in competition with our own banks.

It does not seem to me that this is the proper time to undertake to pass bank legislation for the reason that legislation of this kind passed during these chaotic times might be ill considered and not prove workable during normal times. It seems to me that certain interests are attempting to take advantage of our uncertain financial condition and promote legislation so as to further centralize the control of our banking system. The fact of the matter is that, so far as South Dakota is concerned, confidence is being restored in the banks, which is evidenced by the fact that we have had only three bank closings since November 2, and these three closings were some of the very smallest banks we had in South Dakota; viz, State Bank of Scenic, with deposits of about \$30,000; Midland State Bank, deposits about \$54,000; and the Farmers State Bank of Lesterville, with total deposits of about \$62,000, the total deposits in the three banks being less than \$150,000. The criticism has been that there were too many banks, but I believe that this condition has adjusted itself or will, at least, adjust itself through consolidations and voluntary liquidations. I infer from your letter that you and I are quite in accord with preserving our State banking system and the unit banks.

Some time ago I was urged by representatives of the American Bankers Association to go to Washington to protest against a bill introduced by yourself pertaining to the taxation of national banks. I refused to do this for the reason that I felt that I was a representative of the public rather than of the banks, and especially in view of the fact that the bill had been introduced by yourself I did not feel it proper either to embarrass you or to take a stand with the banks against the public in this matter of taxation.

I sincerely appreciate the invitation you extended to me through Governor Green to appear before the subcommittee on the Glass bill, and I had fully intended coming to Washington pursuant to your invitation but first wanted to obtain the consensus of opinion among the unit banks in South Dakota. I did not realize at the time that this bill would be reported out so soon, otherwise I would have tried to arrange matters so that I could have made the trip without delay, but I was busy at the time in ironing out a matter with one of our former examiners in charge that needed immediate attention, hence my failure to respond as quickly as I should have done. If it should develop at any time that I could be of any assistance in furnishing information with reference to matters affecting the banking situation in South Dakota, I shall be only too glad to come to Washington.

Sincerely yours,

E. A. RUDEN,
Superintendent of Banks.

P. S.—I inclose copy of an article that was sent to me and which apparently was printed in the American Banker in the January 15 issue. Maybe you have seen this article but in any event it is interesting reading.

AND SOME CALL IT "BETTER"

[American Banker, January 15, 1932]

Sundry short-sighted gentlemen of the press and of banking point to our 2,300 bank suspensions in 1931 as a convincing "argument" that branch banking is a better system.

But the last four months has utterly exploded the validity of their argument.

Branch banking as practiced in England and carried on in Canada has faults more glaring and dangerous than any which can be charged against unit banking.

If anything, the branch system is even further than unit banking from that ideal of perfect bank responsibility, so desirable, yet, like other dreams of human perfectibility, probably equally unattainable.

We have our bank closings. The figures tell the story. But branch-banking systems, instead of suspending individually when they are faced with a run, pull the monetary standard of their countries crashingly down when they face the crisis of deflation.

Branch-banking systems are "too big" to fail or to be permitted to fail. They can not suspend to liquidate, as do our American banks, making way for the reorganization of a sound bank or the organization of a new bank. Their liquidation can not be compartmentized and absorbed locally where their credits were spent.

Every Britisher is paying to-day with 30 per cent of his deposits for the "safety" of his branch banking system. Every Canadian is paying for "safety" of his branch-banking system with 20 per cent of his deposits. True, the Britisher and the Canadian have as many pounds sterling or Dominion dollars in the accounts as they had before the crash. However, 20 to 30 per cent of their value has been taken from them by the loss of purchasing power of their funds. True, also, they hope to get full value back. But so do American beneficiaries of individual closed banks, with better reasons, as we see it.

Perhaps you can fool the British and Canadian people into thinking that such a system of mass confiscation of their banked wealth is better. Concentrate the money of a Nation into a few large banks through branch banking if you like. Ignore, if you can, the fact that credit administration is thereby taken from sympathetic local hands and put in the hands of distant city money-market manipulators. Forget, if you can, the fact that another field of the individualistic enterprises to which we owe our American progress is thus handed to a monopoly. Ignore such social and economic implications of branch banking, if you can. But you can not escape the truth that mismanagement of big banks is possible, and when it comes its very momentum is likely to be more costly than we have found it under unit-banking systems. Mistakes can be made by branch bankers. They were made in France, where, after some of the smaller branch banks failed, the government was forced to pour billions of flat francs into the remaining branch-banking systems to keep them alive. French depositors' demands for gold came simultaneously with this government subsidy. The situation in Germany before the moratorium was complicated with branch-bank failures which could only be solved by the use of government guaranties and freezing of deposits. Not only has branch banking given a poor account of itself to its depositors, but countries which have depended upon it have fared badly.

But do we need to look abroad to see the danger which is inherent in the branch bank idea? Our own Government has had to pledge both money and credit to support at least one branch banking situation where poor management policies in the boom had led to weakened depositors' confidence in the depression. Mistakes in banking are being made. And they are bigger and more dangerous in geometric proportion to the scope and size of the banking organizations making them. The fact that the error may hinge upon Government fiscal policy as well as banking, only emphasizes the fact that bigness of banks is a liability to governments rather than an asset in times of crisis.

London made such a mistake. It was a banking and credit blunder. Every moneyed person in the British Empire is to-day paying the price of that mistake. The folly was too big to be absorbed in the reorganization or liquidation of one or more banks. Closing even one big branch bank would have precipitated a national smash. Instead, the British Government and bankers have charged the cost of their mistakes to the entire wealth of the country. The banks simply went off the gold standard. Unit banking can not exist without

the implication that some banks will be run better than others. But unit bankers can look forward to the hope that through the cooperative effort toward better bank management as expressed in American Bankers Association work, in Federal reserve membership, local clearing-house associations, and the like, the percentage of mismanagement and the percentage of victims of Government mismanagement can be reduced to a smaller and smaller figure.

Branch banking systems can not be operated without facing the danger that mistakes at headquarters will plunge the whole country disastrously off its gold base.

Only a fool can delude himself into the belief that any guaranty of bank deposits is possible.

His folly is no less if he worships the guaranty of deposits idea under the guise of branch banking.

FARMERS STATE BANK,
Westport, S. Dak., March 26, 1932.

HON. PETER NORBECK,
United States Senate, Washington, D. C.

DEAR MR. NORBECK: The provision in the Glass bill restricting branch banking to those States that permit State branch banking should be sustained. There is going to be a fight on this restriction—the branch, chain, and group banking interests in the country are going to bring their influence to bear against this restriction in the hope that it will provide another wedge into the dream of national branch banking over the entire country.

States rights should be held inviolate; the people in each State should have the power to say whether they want branch banking. The big argument in favor and which is being stressed by those interested is in safety, but the record of failures of branch and chain banking in this country the past few years amply demonstrates the fallacy of that theory. Unit banks can be and many are just as safe as a bank should be; they have the interest of their own communities at heart. Witness this bank which in the 12 years under my control has been one of the few in the country that has never had to borrow any money, and to-day we are taking care of the legitimate requirements of our customers.

Branch banking in the final analysis will bring on economic stagnation, stifle individual enterprise, and throttle the "little fellows," the farmers and small tradespeople. Why all this howl about losses to bank depositors? The percentage of loss has been less than to most any other class of investor. Let's take, for sake of argument, the cases of, say, four people, who three years ago each had \$5,000 to invest. One put his money into a farm, one into what he had been led to believe were sound bonds, one into a first-class farm or city mortgage, and last put his into a bank. We will say the bank failed. Who was the worst off? The record will show that the man who put his money into the bank sustained, in the majority of cases, the least loss of any.

The big banking interests of the country are simply using the present economic chaos into which the whole world finds itself as an excuse to seize control of the banking business, to centralize the money power in the East for the benefit of so-called big business and to the exclusion and disregard of the agricultural sections of the country. If this succeeds it will mean ruin to millions of people and the stifling of individual enterprise. If you have any doubt of this you might take a trip into Canada, as I have on two different occasions, and talk with people in that country—a country that is just as wealthy in national resources as we are—you can come to but one conclusion, and that is that their whole economic and individual development has been permanently impaired—due, for the most part, to their system of branch banking. The small tradesman, the merchant, and the farmer simply hasn't a chance. If, finally, we have nation-wide branch banking in this country, then we are coming to the same condition—just as surely as the sun rises in the morning, and nation-wide branch banking is what we are coming to unless the people wake up in time. There have been losses under our present form of banking—losses which no system of banking can entirely overcome—but rather those losses than the loss of our individual initiative and economic progress that is bound to follow the abolition of "independent" banking.

I am going to watch with much interest the scrap that is bound to come up over the restriction in the Glass bill to which I have referred.

Yours very truly,

DON W. DE VEY.

The **CHAIRMAN**. We will adjourn to meet at 2.30 in the Interstate Commerce Committee Room in the Capitol, Senator Couzens's room, where we met yesterday afternoon, and the first witness will be Mr. Eugene Meyer, governor of the Federal Reserve Board.

(Accordingly, at 12.25 o'clock p. m., the committee was in recess until 2.30 o'clock p. m. of the same day.)

AFTER RECESS

The committee reconvened at 2.30 o'clock p. m. in the hearing room of the Interstate Commerce Committee in the Capitol, at the expiration of the recess, Senator Peter Norbeck presiding.

The **CHAIRMAN**. The committee will come to order. Mr. Meyer, you may take a seat at the committee table opposite the committee reporter.

STATEMENT OF EUGENE MEYER, GOVERNOR FEDERAL RESERVE BOARD, WASHINGTON, D. C.

Mr. **MEYER**. Mr. Chairman and gentlemen of the committee, if I may, I should like to have the opportunity to present the matters that I have here without interruption, and then I will be ready to answer questions so far as I can.

The **CHAIRMAN**. I think the members of the committee will be perfectly willing to have you do that.

Mr. **MEYER**. I might add that I have a special reason for making this request, because I shall be reading from a letter to the chairman of this committee and from the memorandum attached to the letter, expressions which are the unanimous views of the members of the Federal Reserve Board, and if I were answering questions during the reading of these communications I might not be able to speak for the Board.

The **CHAIRMAN**. But you are perfectly willing to answer questions propounded by the members of the committee afterwards?

Mr. **MEYER**. I shall be perfectly willing to answer any questions I can.

The **CHAIRMAN**. You will proceed then.

Mr. **MEYER**. I shall first read a letter I am sending to you to-day on behalf of the Federal Reserve Board. [Reading.]

MARCH 20, 1932.

HON. PETER NORBECK,

*Chairman Committee on Banking and Currency,
United States Senate, Washington, D. C.*

DEAR SENATOR NORBECK: On March 17, 1932, I received a letter from Senator Glass inclosing copies of Senate Bill 4115, and stating that the Banking and Currency Committee would be glad to have the Federal Reserve Board make any comments or suggestions that in its judgment would seem desirable. Accordingly, there is inclosed herewith for the consideration of your committee a memorandum containing the board's comments and recommendations.

The subjects dealt with in the bill may be classified under three general heads: (1) Those relating more directly to the Federal Reserve Board and the reserve banks; (2) those concerning primarily member banks, and (3) those dealing with affiliates of member banks.

The Federal Reserve Board is in sympathy with the purpose of the bill to strengthen the supervision of the Federal reserve system over general credit conditions and to invest the Federal reserve authorities with certain disciplinary powers in relation to banks that pursue unsafe and unsound policies or abuse the privileges of membership. The board's recommendations on this

subject are incorporated in its proposed revision of sections 3 and 29 of the bill.

With respect to the section of the bill dealing with open-market operations, the board calls attention to the fact that there is already in existence an open-market committee on which each of the Federal reserve banks has representation. This has come about as the result of natural development. The board believes that it would be inadvisable to disturb this development by crystallizing into law any particular procedure. The board believes that nothing further is necessary or advisable at this time than an amendment clarifying its power of supervision over open-market operations of the Federal reserve banks and their relationships with foreign banks, as set out in the memorandum attached.

The board is not in sympathy with the provisions of the bill discriminating against member bank collateral notes. Experience shows that the particular instrument on which Federal reserve credit is obtained is not an adequate test of the use to be made by the member bank of the proceeds of the credit and that an attempt to control speculation through restrictions on member bank collateral notes would not be effective in accomplishing the purpose of this section of the bill. Indeed, it probably would interfere seriously with the convenient and economical operation of the system. In this connection, the Federal Reserve Board desires to renew the recommendation made in its annual reports for several years, that the maturity for which advances may be made to member banks on their promissory notes secured by paper which is eligible for discount be increased from 15 to 90 days. Such an amendment would be especially helpful to country banks.

The board is of the opinion that the adoption of a system of reserves based on velocity of accounts as well as on their volume, as recommended by the System's Committee on Reserves, would be an important step in strengthening the influence that the Federal Reserve System could exert in the direction of sound credit conditions. The section of the bill dealing with reserves would accentuate rather than reduce the inequalities that have grown up in the distribution of reserves between different classes of member banks. The board also believes it should not be overlooked that this section of the bill would exert a tightening influence on credit conditions at times when it would be contrary to the public interest.

The board is in favor of establishing a liquidating corporation, but proposes to limit the scope of its operations to member banks and suggests a different method of financing it, together with certain changes in the provisions for its administration.

If the section on branch banking is enacted in the form proposed in the bill, it is suggested that certain sections of existing law be modified so as to bring them into harmony with the purposes indicated in this section of the bill.

With respect to affiliates, the board believes that important reforms to be accomplished at the present time are the granting of power to the supervisory authorities to obtain reports and to make examinations of all affiliates of member banks and the prescribing of limitations on the loans that a member bank may make to its affiliates. The board realizes that many evils have developed through the operation of affiliates connected with member banks, particularly affiliates dealing in securities. The attached memorandum contains a draft of a provision for the separation of such affiliates after a lapse of three years.

The board takes the view that legislation further materially restricting the character of member bank loans and investments is not desirable at a time when the country's banking system is going through a period of severe readjustment. Some of the provisions of the proposed bill would have a tendency to bring about further contraction of credit and thus retard the recovery of business. It is for these reasons that changes in a number of sections of the bill are suggested.

It should be recognized that effective supervision of banking in this country has been seriously hampered by the competition between member and nonmember banks, and that the establishment of a unified system of banking under national supervision is essential to fundamental banking reform.

Copies of this letter and the inclosed memorandum are being sent to Senator Glass, and the board will be glad to supply you with copies for the convenience of each member of your committee.

Very truly yours,

EUGENE MEYER, *Governor.*

Mr. MEYER. The memorandum which I have here, and of which the members of the committee will receive copies for their convenience while sitting here at the table, contains detailed comments and suggestions of amendment of the form of the bill, some of which I should like to read to the committee. Concerning some of these matters I shall perhaps wish to make some additional comments as I go along. As to others, I shall not take up the time of the committee to read or discuss them but shall merely submit them as a part of the memorandum.

Senator COUZENS. As you conclude each paragraph do you mind questions, I mean after the paragraph has been concluded?

Mr. MEYER. No. But, having in mind that this is the unanimous recommendation of the board, and that when I answer questions I can not always anticipate what replies the board would make, you will understand that I can only answer in my personal capacity.

Senator COUZENS. But after you conclude each section that you intend to discuss here, it seems to me the members of the committee would perhaps like some amplification.

Senator WALCOTT. You mean, Senator Couzens, after each section that he discusses.

Senator COUZENS. Yes.

Mr. MEYER. This is not a complete comment on each section of the bill S. 4115, you will understand, Senator Couzens. This is a memorandum of particular points upon which the board desired to express its views.

Senator COUZENS. Then are we to understand that as to those paragraphs of the bill you do not comment on they are satisfactory to the board?

Mr. MEYER. Well, there are some that you might describe as satisfactory, and there are others on which the board did not, for one reason or another, undertake to express its views.

Senator COUZENS. Then I understand that where you do not comment on a section or paragraph of the bill, the board does not desire to express its views, is that correct?

Mr. MEYER. That is correct, as the memorandum expresses the unanimous opinion of the board, and I think almost all of the important sections of the bill are discussed.

The CHAIRMAN. You may proceed, Governor Meyer.

Mr. MEYER. These are comments and recommendations regarding the bill S. 4115, and all references are to sections, pages, and lines in the form in which the bill was introduced on March 14 (calendar day, March 17), 1932.

Section 2: This section defines affiliates and upon its scope depends in a large measure the scope and effect of all provisions of the bill relating to affiliates.

While the definition contained in the bill mentions certain specific types of institutions which are frequently affiliated with member banks, the words "or a corporation," in line 4, on page 2, make it applicable to corporations of any character which are affiliated with member banks in any of the ways described in the succeeding paragraphs of the definition.

It is believed that the most satisfactory solution of this problem is to make the definition very broad but, in dealing with affiliates, to observe the following principles: (1) To require them to make

reports and to submit to examination at the discretion of the board or the comptroller; (2) to limit the loans that can be extended to an affiliate by a member bank; (3) to prohibit the tying up of capital stock of an affiliate with the capital stock of a member bank. In favoring these limitations, the board has in mind that it may not be desirable to abolish all the existing relationships between member banks and their affiliates, but that it is desirable to protect the operations of the member banks from being unduly influenced by their affiliates. Recent experience has demonstrated that operations of the affiliates at times have unfavorable effects on the condition of member banks.

With these principles in mind, it is recommended that the definition of "affiliates" be broadened by eliminating from paragraph (b) in lines 1 to 4, page 2, all references to specific types of corporations, and by inserting other words which would make the definition applicable not only to corporations but to business trusts, associations, or other similar organizations, regardless of the type of business in which they are engaged.

Senator TOWNSEND. Governor Meyer, do you suggest any language in there?

Mr. MEYER. The memorandum farther down contains a suggestion of the language.

Senator TOWNSEND. All right.

Mr. MEYER. This question of course is one of the most important and interesting in the bill. There are certain possible affiliates of banks which are now provided for by Federal law, such as national agricultural corporations, to the capital of which the banks are expressly authorized to subscribe; and there are several other categories of affiliates which may be considered entirely legitimate and proper.

Senator COUZENS. Will you name one for our information?

Mr. MEYER. Well, I would suggest, for instance—

Senator FLETCHER (interposing). Looking at your memorandum, Governor Meyer, would you mind reading your substitute in that connection?

Mr. MEYER. All right. Certain other changes in the phraseology of the definition are also suggested for the purpose of clarifying them. The changes suggested are as follows:

1. On page 2, change lines 1 to 4, inclusive, to read as follows:

(b) The term "affiliate" includes any corporation, business trust, association or other similar organization—

2. In lines 9, 11, and 22 on page 2, strike out the words "managing officers" and substitute in lieu thereof the words "persons exercising similar functions."

3. In lines 9 and 18 on page 2, and in line 3 on page 3, strike out the words "annual meeting" and substitute in lieu thereof the word "election."

There are other references to the question of affiliates further on in this memorandum, and if it is agreeable to the committee perhaps we can discuss that question again later.

The CHAIRMAN. Very well. You may proceed.

Mr. MEYER. Section 3: The Federal Reserve Board understands that the principles underlying section 3 of the bill are (1) that discounting at the Federal reserve banks is a privilege and not a right;

(2) that the Federal reserve system has the responsibility of keeping itself informed about the use of bank credit; (3) that the power of Federal reserve banks to withhold credit accommodations should be used to discourage unsound banking practices; and (4) that the Federal Reserve Board should have power to suspend a member bank from the use of Federal reserve credit facilities. The board is in sympathy with these principles.

For the purpose of accomplishing these objectives, a substitute for section 3 is suggested. This substitute includes a revision of the paragraph of section 4 of the Federal reserve act which now reads as follows:

Said board shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and shall, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements, and accommodations as may be safely and reasonably made with due regard for the claim and demands of other member banks.

In this revision the word "may" is substituted for "shall" and the remaining language of the section is made somewhat more general than in the bill.

Member banks as a rule do not borrow to relend, but to make up deficiencies in reserves arising from withdrawals of deposits or from other causes. It is, therefore, usually impossible to say that a loan to a member bank is granted for this or that specific purpose. However, it would be possible to determine whether the loan and investment policies of a bank are inconsistent with the purposes of the Federal reserve act, and, if so, to refuse accommodation to such bank or in aggravated cases to suspend it from the privilege of using the system's credit facilities. In this connection attention is invited to the fact that section 4 of the Federal reserve act requires the chairman and Federal reserve agent at each Federal reserve bank to "make regular reports to the Federal Reserve Board" and to "act as its official representative for the performance of the functions conferred upon it by" the Federal reserve act.

It is recommended that section 3 of the bill be changed to read as follows:

SEC. 3. The paragraph of section 4 of the Federal reserve act, as amended, which begins with the words, "Said board shall administer the affairs of said bank fairly and impartially," is amended and reenacted to read as follows:

"Said board of directors shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and may, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements, and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks, the maintenance, of sound credit conditions and the accommodation of commerce, industry, and agriculture. The Federal Reserve Board may prescribe regulations further defining within the limitations of this act the conditions under which discounts, advancements, and accommodations may be extended to member banks. Each Federal reserve bank shall keep itself informed of the general character and amount of the loans and investments of its member banks with a view to ascertaining whether undue use is being made of bank credit for the speculative carrying of or trading in securities, real estate, or commodities, or for any other purpose inconsistent with the maintenance of sound credit conditions; and, in determining whether to grant or refuse advances, rediscounts, or other credit accommodations, the Federal reserve bank shall give consideration to such information. The chairman of the Federal reserve bank shall report to the Federal Reserve Board any such undue use of bank credit by any member bank, together with his recommendation. Whenever, in the judg-

ment of the Federal Reserve Board, any member bank is making such undue use of bank credit, the board may, in its discretion, after reasonable notice and an opportunity for a hearing, suspend such bank from the use of the credit facilities of the Federal reserve system and may terminate such suspension or may renew it from time to time."

SEC. 4. It is recommended that this section be omitted. It prohibits banks that belong to a group or a chain from voting for Federal reserve bank directors. The wording of the section is such as not to confine the prohibition to group and chain banks, however, but to include all banks that are not controlled entirely by locally resident stockholders. Since the stock of many important banks is widely owned throughout the country, this might restrict the voting privilege to smaller and less important banks that are owned by local stockholders. It is to be feared that this section would bar from participation in the selection of Federal reserve directors many of the better managed banks.

SEC. 5. This section would amend the first paragraph of section 7 of the Federal reserve act so that, after the payment of expenses and dividends, all of the net earnings of a Federal reserve bank over and above any amounts necessary to restore its surplus to the amount on December 31, 1931, would be paid to the Federal liquidating corporation. The amendment is also worded in such a way as to prevent the payment of any dividends out of surplus and to prevent the payment of dividends whenever the surplus of a Federal reserve bank is less than it was on December 31, 1931.

A different method of financing the liquidating corporation is proposed and will be discussed under the appropriate section. For this reason a modification of section 5 is suggested which would not change the provisions of the present law in regard to the surplus of the Federal reserve banks, but would authorize the Secretary of the Treasury to use the franchise tax received from the Federal reserve banks for the purpose of supplementing the funds of the corporation.

As changed, section 5 of the bill would read as follows:

SEC. 5. The second paragraph of section 7 of the Federal reserve act, as amended, is amended to read as follows:

"The net earnings derived by the United States from Federal reserve banks shall, in the discretion of the Secretary of the Treasury, (1) be used to supplement the gold reserve held against outstanding United States notes, or (2) be applied to the reduction of the outstanding bonded indebtedness of the United States under regulations to be prescribed by the Secretary of the Treasury, or (3) be invested in debentures or other such obligations of the Federal Liquidating Corporation. Should a Federal reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts, dividend requirements as hereinbefore provided, and the par value of the stock, shall be paid to and become the property of the United States and shall be similarly applied."

Section 6: In order that reports of affiliates of State member banks may be required only when deemed necessary by the Federal Reserve Board and also in order that suitable provision may be made for the examination of affiliates of State member banks when deemed necessary, it is recommended that section 6 of the bill be changed to read as follows:

SEC. 6. Section 9 of the Federal reserve act, as amended, is further amended by adding at the end thereof two paragraphs reading as follows:

"Whenever it shall be deemed necessary in order to obtain adequate information regarding the relations between any bank admitted to membership

under the provisions of this section and its affiliates or the effect of such relations upon the management or condition of such bank, it may be required under rules and regulations prescribed by the Federal Reserve Board to obtain and furnish such reports as to any or all of its affiliates as may be called for. Each such report shall contain such information and shall be submitted at such time as may be specified in the call therefor. Any member bank which fails to furnish any report of an affiliate when and as required shall be subject to a penalty of \$100 for each day during which such failure continues. Such penalty may be assessed by the Federal Reserve Board, in its discretion, and, when assessed, may be collected by the Federal reserve bank by suit or otherwise.

"Any examiner selected or approved by the Federal Reserve Board may examine any affiliate of any bank admitted to membership under the provisions of this section when it shall be deemed necessary in order to inform the Federal Reserve Board or the Federal reserve bank of the relations of such affiliate with such member bank or of the effect of such relations upon the management or condition of such member bank. The examiner making the examination of any such affiliate shall have power to make a thorough examination of all the affairs of the affiliate, and in doing so he shall have power to administer oaths and to examine any of the officers, directors, employees, and agents thereof under oath, and to make a report of his findings to the Federal Reserve Board or to the Federal reserve bank. The expenses of any examination made under the provisions of this paragraph may, in the discretion of the Federal Reserve Board, be assessed against the affiliate examined and, when so assessed, shall be paid by the affiliate examined. If such affiliate shall refuse to pay such expenses or shall fail to do so within sixty days after the date of such assessment, then such expenses may be assessed against the affiliated member bank and, when so assessed, shall be paid by such member bank: *Provided, however,* That, if the affiliation is with two or more member banks, such expenses may be assessed against, and collected from, any or all of such member banks in such proportions as the Federal Reserve Board may prescribe. If any affiliate of a bank admitted to membership under the provisions of this section shall refuse to permit an examiner to make an examination of such affiliate or refuse to give any information required in the course of any such examination, the member bank with which it is affiliated shall be subject to a penalty of not more than \$100 for each day that any such refusal shall continue. Such penalty may be assessed by the Federal Reserve Board in its discretion and, when so assessed, may be collected by the Federal reserve bank by suit or otherwise."

Section 7. If this section is adopted in its present form, certain changes should be made in the text for the purpose of clarification and of providing for certain matters not now covered in the bill which will be referred to at the appropriate places.

For the purpose of clarification, it is suggested that subsection (b) be amended as follows:

1. In lines 6, 11, and 12, on page 8, it is suggested that the word "appointive" be inserted before the word "member."

2. In line 13, on page 8, it is suggested that after the words "twelve years" there be inserted the words "from the expiration of the term of his predecessor."

In order that the domicile of the board may be fixed for legal reasons, and in order that provision may be made for a chairman of the board, it is suggested that the following be inserted at the beginning of line 23, on page 8:

The principal offices of the board shall be in the District of Columbia. At meetings of the board, the governor shall preside as chairman, and, in his absence, the vice governor shall preside. In the absence of both the governor and the vice governor, the board shall elect a member to act as chairman pro tem.

If the authority of the Secretary of the Treasury to assign quarters to the Federal Reserve Board is repealed, it would seem that

the board should be authorized to purchase or construct a building for its own use and that, in the interest of convenience and efficiency, space should be provided in such building for the Comptroller of the Currency and his staff and for the proposed Federal liquidating corporation. For this purpose, it is suggested that the following be added at the end of section 7 of the bill:

(d) Section 10 of the Federal reserve act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

The Federal Reserve Board is authorized and empowered to acquire by purchase, condemnation or otherwise, a building located in the District of Columbia which will provide suitable and adequate offices wherein the functions of the board and the Comptroller of the Currency may be carried on, or to acquire by purchase, condemnation or otherwise, such site located in the District of Columbia as it may deem necessary and to cause to be constructed thereon a building which will provide suitable and adequate offices for the purposes of the Federal Reserve Board and the Comptroller of the Currency, and to maintain, repair, enlarge or remodel any building so acquired or constructed. The Federal Reserve Board may assign offices in any such building for the use of the Comptroller of the Currency and the Federal liquidating corporation without making any charge for the use of such offices, and nothing contained in the act of June 3, 1864, or in section 831 of the Revised Statutes (title 12, sec. 13, U. S. C.), or in any other provision of law, shall be construed as preventing the Comptroller of the Currency from making full use of any offices so assigned and from keeping therein the records and all other valuable things belonging to his department. The Federal Reserve Board may levy upon the Federal reserve banks, in proportion to their capital stock and surplus, assessments sufficient to defray all costs and expenses incurred under the provisions of this paragraph.

Whether the Secretary of the Treasury should continue to serve ex officio as a member and chairman of the board, is a question that the board, I think, in general is inclined to feel should be decided primarily by the committee and the Congress. I think the board feels it might be a little out of place for it to make any suggestions concerning its own composition.

I will say, however, that it is a rather interesting question. I think the board feels there are some definite advantages in having the secretary present at meetings and, on the other hand, there would be perhaps some advantages in his absence. I had a little discussion with Senator Glass on the subject when he asked me some months ago how I felt about it, and I stated that I had no strong feelings. As a matter of fact, during the time I have been governor of the board, I have found nothing to object to in the presence of the Secretary of the Treasury as a member of the board. On the other hand, it is easy enough to see that the board, having as its chairman ex officio a man as powerful and as important as the Secretary of the Treasury, might be suspected of being unduly influenced by him; and yet I know, gentlemen of the committee—

Senator GLASS (interposing). Of course it is never so.

Mr. MEYER. Well, I know it is so, because I know you said you did it. But it has not been so in the last year and a half.

Senator GLASS. Not since you have been governor, no. [Great laughter in the room.]

Mr. MEYER. Well, I just have this thought about it from the point of view of public policy: I can see all the disadvantages of having such an important official of the Government as chairman ex officio. On the other hand, if the board, with its power over the banking

and financial situation of the country, did not have in its membership the kind of representation that the Secretary of the Treasury is intended to provide, it is possible that, when some policy that was unpopular but perhaps very sound was in process of being enforced, the criticism would be made that this was a board of merely bureaucratic officials, set aside in the Government and independently exercising arbitrary power, with no one on the board reflecting the public point of view that an official such as the Secretary of the Treasury might be expected to have. In other words, while it is easy to see a disadvantage in the existing state of affairs, I think you have to consider all of the possibilities that might arise under new conditions.

Senator GLASS. Well, you will recall that when the Federal reserve bill was enacted into law one of the most vehement objections to it was by the American Bankers' Association, and particularly to that provision that put the Secretary of the Treasury on the board. They called it a political board, and some of them do now.

Mr. MEYER. Well, that is the disadvantage of the presence of the Secretary, and, laying aside any personalities as affecting the late Secretary or the present Secretary or any present member on the board, I can see great advantages in a separation. But I want to say this, that while the Secretary's membership is always thought of in the terms of the Secretary of the Treasury having access to the board's counsels, and having the ability to influence its policy in a direction advantageous to Government finance, I see, too, that direct contact with the Secretary of the Treasury, on behalf of the board's interest from a banking point of view in the Treasury's policies, is a considerable advantage. I do not think it is a one-sided matter. I should say that we feel as free to express the banking point of view on Treasury policies when the Secretary is present in the board meetings as the Secretary does to express his views from the Government's financial point of view about banking policies.

Senator GLASS. I am glad that that has been so radically changed since I was Secretary of the Treasury.

Mr. MEYER. Well, you can see that there is some point to that possibility, because after all the banks of the country have a very direct interest in the policies of Government finance.

I was wondering whether on this particular subject you would care to consider perhaps an intermediate course, for instance, perhaps to make the Secretary of the Treasury an ex officio member of the board without a vote and eliminate him from the chairmanship. That would provide a normal and natural means for regular conferences, without, I should say, the suspicion of undue influence. However, that is merely a suggestion for your consideration. I think there is considerable advantage from the banking point of view in having the Secretary on the board, and I am not thinking of any advantage to the Secretary of the Treasury as head of the Government's financial department.

Senator FLETCHER. There is no difficulty about the board being in frequent conference and contact with the Secretary of the Treasury, is there?

Mr. MEYER. Well, of course, if this bill were enacted and the board moved out of the building, if we wanted to have a conference, should

we send for the Secretary of the Treasury to come over to see us? Or should we ask for an appointment with the Secretary when we might be allowed to see him? It might be a rather embarrassing matter, whereas if he were an ex officio member without a vote he would attend when pending matters were interesting to him, and when he had the time, and he would be available in the normal way. In other words, there would not be any discussion about how to arrange meetings.

Senator FLETCHER. It seems to me that is a mere matter of location of the offices.

Mr. MEYER. It is more than that. I do not think the Secretary of the Treasury, who is a very important officer in the Government, would care to be sent for by the various boards and bureaus of the Government around Washington.

Senator GLASS. No, and I sent for the board.

Mr. MEYER. And you were the Secretary of the Treasury then. But I am saying if the Secretary of the Treasury were not a member of the board he might not send for the board, because the board might not feel particularly responsive to his calls. I do not know that the board would respond to a call from the Secretary of the Treasury if he were not a member of the board and had no official relationship with it.

Senator GLASS. You make yourself very skillfully persona grata.

Mr. MEYER. Well, I am only trying to throw a little light on the discussion. I have not thought very much about this, although it is interesting, I admit.

Senator FLETCHER. It seems to me if we are going to put him on the board we should do so and not as a figurehead.

Mr. MEYER. Well, not as a figurehead, but by following that suggestion he would have a natural way for conference.

Senator GLASS. What about the Comptroller of the Currency?

Mr. MEYER. This report does not discuss that, and your bill did not refer to it, so we did not comment on it. Personally I think it is fair to say that a good many members of the board, although I would not say all, because we have not taken a vote on it, have the feeling that there is no need of, and no great benefit in, the presence of the Comptroller of the Currency on the board. He is such a busy individual that he has very little time to give to the affairs of the board, except at meetings which he attends only occasionally, and then probably for only a part of the meetings.

Senator GLASS. How many times in the year would your minutes show the Secretary of the Treasury attended the meetings of the board?

Mr. MEYER. Do you mean in the last year?

Senator GLASS. Well, in any one year.

Mr. MEYER. Over what period do you mean?

Senator GLASS. In a year.

Mr. MEYER. Well, I have only been there for a year and a half. Mr. Mellon only attended meetings as a rule when we asked him to for the purpose of making up a quorum. Since Mr. Mills has been Secretary of the Treasury, he has frequently attended and is interested in the discussions. He attends whenever he can—I should say, whenever he has the time.

Senator GLASS. Of course you know that we have discussed this matter for quite a period of time.

Mr. MEYER. How do you mean?

Senator GLASS. I mean that we have not sprung it on an unsuspecting public.

Mr. MEYER. No, but the idea had not come to me previously that the Secretary of the Treasury might be a nonvoting member of the board.

Senator GLASS. Do you mean unofficial observer?

Mr. MEYER. Well, as an ex officio member of the board without a vote, but eliminating him from the chairmanship as you propose. I am not urging it. I am not recommending it, and the board did not discuss that in this report, and therefore it is merely a suggestion made now for your consideration.

Senator GLASS. Well, the subcommittee did not regard it as vital.

Mr. MEYER. How was that?

Senator GLASS. I say, the subcommittee did not regard it as vital.

Mr. MEYER. No, I so understand.

The CHAIRMAN. You may continue your statement, Mr. Meyer.

Mr. MEYER. Section 8: The purpose of this section is to prevent the undue use of bank loans for speculation in securities. It is believed that this is sufficiently covered in section 3 and, therefore, the omission of section 8 is recommended.

Section 9. In accordance with the principles indicated in the discussion of section 2, it is recommended that section 9 of the bill be changed to read as follows:

"SEC. 9. The Federal reserve act, as amended, is amended by inserting between sections 23 and 24 thereof the following new section:

"SEC. 23(a). No national banking association and no State member bank shall (1) make any loan or any extension of credit to, or purchase securities under repurchase agreement from, any of its affiliates, or (2) invest any of its funds in the capital stock, bonds, or other obligation of any such affiliate, or (3) accept the capital stock, bonds, or other obligations of any such affiliate as collateral security for advances made to any individual, partnership, association, or corporation; if, in the case of any such affiliate, the aggregate amount of such loans or extensions of credit, repurchase agreements, investments, and advances against such collateral security will exceed 10 per centum of the capital stock and surplus of such national banking association or State member bank; or if, in the case of all such affiliates, the aggregate amount of such loans, extensions of credit, investments, and advances against such collateral security will exceed 20 per centum of the capital stock and surplus of such national banking association or State member bank: *Provided, however,* That nothing in this section, or in any section of the banking act of 1932, shall be construed as authorizing member banks to invest their funds in stock otherwise than as specifically authorized by existing law.

"Each loan or extension of credit to an affiliate within the foregoing limitations shall be secured by collateral having a market value at the time of making the loan or extension of credit of at least 20 per centum more than the amount of such loan: *Provided,* That this requirement shall not apply to loans or extensions of credit on

the security of obligations of the United States Government, Reconstruction Finance Corporation, Federal Intermediate Credit Banks, or Federal land banks, or on the security of notes, drafts, bills of exchange, or acceptances eligible for discount or purchase by Federal reserve banks: *And provided further*, That when any loan is made on the security of obligations of any State or political subdivision or agency thereof such obligations shall have a market value at the time of making the loan of at least 10 per centum more than the amount of such loan. A loan or extension of credit to a director, officer, clerk, or other employe or any representative of any such affiliate shall be deemed a loan to the affiliate to the extent that the proceeds of such loan are used for the benefit of, or transferred to, the affiliate.

“ The provisions of this section shall not apply to any affiliate of such national banking association or State member bank, (1) the sole function of which is to hold its banking house or houses and the site or sites thereof, (2) the sole function of which is to conduct a safe deposit business, (3) in the capital stock of which such bank has been authorized to invest pursuant to section 25 of the Federal reserve act, (4) organized under section 25(a) of the Federal reserve act, or (5) transacting only the business of an agricultural credit corporation or live stock loan company; but as to such affiliates member banks shall continue subject to the provisions of existing law limiting the amounts which they may lend to, or invest in the stock or other obligations of, such corporations.”

SEC. 10. This section of the bill deals with two separate and distinct subjects, (1) open market operations of the Federal reserve banks, and (2) the proposed Federal liquidating corporation. For convenience, these subjects, will be discussed separately.

Open market operations: The first part of Section 10 would establish a Federal open market committee along the lines of the existing open market policy conference which functions as a piece of administrative machinery without specific legal status.

The statement in paragraph (b) of section 10 which says that, “ No Federal reserve bank shall engage in open market operations, except after approval and authorization by the committee,” appears to be too rigid. It deprives an individual reserve bank of all authority to make purchases in the open market except after obtaining the consent of both the board and the committee. The open market committee would have no authority to act without approval of the board and the board would have no authority to act without approval of the committee. This would result in the possibility of obstruction of any system program and would tend to make the operation of the Federal reserve system less timely and less efficient.

Lines 19 to 23 in paragraph (c) on page 12 of this section would incorporate into law a principle which the Federal Reserve Board has adopted in practice.

The following substitute for the first part of section 10 of the bill is suggested:

SEC. 10. Section 14 of the Federal reserve act, as amended, is further amended by striking out the words ‘ Every Federal reserve bank shall have power;’ and inserting in lieu thereof the following:

“ Subject to such regulations, limitations, restrictions and procedure as the Federal Reserve Board may prescribe, every Federal reserve bank shall have power:”

"Section 14 of the Federal reserve act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

"The time, character and volume of all purchases and sales in the open market under this section shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country."

Senator GLASS. Governor, wouldn't that proposed amendment abrogate the right of a Federal reserve bank to initiate the discount rate and transfer it to the Federal Reserve Board?

Mr. MEYER. I think not, Senator Glass. After looking at it again I would say it concerns open market operations: I do not think it would, but I should like to ask our counsel.

Mr. WYATT. I do not think it would.

Mr. MEYER. Our counsel is sitting here behind me, and he tells me it would not.

Senator GLASS. I am very much of opinion it would, and that is a bitterly contested proposition.

Mr. MEYER. You want to maintain the initiative in the banks?

Senator GLASS. Yes.

Mr. MEYER. It has been our policy to do that. I have attended meetings where the directors of banks have been discussing rates, and never had anything to say about it at all.

Senator GLASS. But you know it was a bitterly controverted proposition.

Mr. MEYER. Yes.

Senator GLASS. And that it created quite a sensational dispute?

Mr. MEYER. I am in entire sympathy with your view on that, Senator Glass, and am quite sure that we were not in the slightest degree intending that there should be any change. And our counsel advises me that he thinks it does not change that proposition.

Senator GLASS. Well, I was so certain of it that the technician of this committee having embodied that in the bill I had it stricken out.

Mr. MEYER. Well, of course it is worth studying from that point of view, but I think it is perfectly innocuous in that respect. I should like to have it looked into a little more fully by our counsel, and will write you a memorandum on that, for the benefit of the committee, if you and they so desire.

Senator GLASS. I am willing to be convinced.

Mr. MEYER. All right, Senator Glass, we will try to furnish you a basis for a sound conviction.

The CHAIRMAN. You may continue your statement, Governor Meyer.

Mr. MEYER. Federal liquidating corporation: The other part of section 10 deals with the proposed Federal liquidating corporation, and there is submitted a proposed substitute for the section as drafted in the bill. The substitute would confine the benefits of the liquidating corporation to member banks. Provision is made for assistance to nonmember banks in the Reconstruction Finance Corporation act, and it would render membership in the system more attractive if the benefits of the corporation were confined to member banks. In the substitute it is proposed that \$100,000,000 of the capital of the liquidating corporation be subscribed by the Treasury. This subscription to capital may be considered as being derived from the franchise tax previously paid to the Treasury by the reserve banks.

In addition, it is proposed that the corporation be authorized to issue debentures up to twice the amount of its subscribed capital and that the Federal reserve banks be given authority to purchase those debentures up to one-fourth of their surplus. This is not a propitious time to ask the member banks to contribute to the liquidating corporation. The banks are going through a very difficult period and to tax them for this purpose would be a considerable hardship on them.

In order to make the operations of the corporation more easily manageable, it is proposed that the directorate be comprised of 5 members instead of 14 as proposed in the bill.

For the reasons which have been stated the following separate section on the Federal liquidating corporation has been drafted:

SEC. 5A. The Federal reserve act, as amended, is further amended by inserting between sections 28 and 29 thereof the following new section:

SEC. 28A. (a) There is hereby created a Federal liquidating corporation (hereafter referred to as the "corporation") for the purpose of making loans on, or purchasing and liquidating as hereinafter provided, all or any part of the assets of any member bank for which a receiver has been appointed. The term "receiver" as used in this section shall mean a receiver of a national bank, and a receiver, liquidating agent, commission, person, or other agency charged by State law with the responsibility and the duty of winding up the affairs of an insolvent State member bank.

(b) The management of the corporation shall be vested in a board of directors consisting of five members, one of whom shall be the Comptroller of the Currency, one a member of the Federal Reserve Board designated by the board for the purpose, and three selected annually by the governors of the 12 Federal reserve banks under such procedure as may be prescribed by the Federal Reserve Board.

(c) The corporation shall have a capital stock of \$100,000,000, all of which shall be subscribed by the United States of America and payment for which shall be subject to call in whole or in part by the board of directors of the corporation.

There is hereby authorized to be appropriated out of any money in the Treasury not otherwise appropriated the sum of \$100,000,000 for the purpose of making payments upon such subscription. Receipts for payments by the United States for or on account of such stock shall be issued by the corporation to the Secretary of the Treasury and shall be evidence of the stock-ownership of the United States.

Any Federal reserve bank may purchase and hold any debentures or other such obligations of the corporation in an amount not exceeding one-fourth of the amount of its surplus fund.

(d) The corporation shall have power—

First. To adopt, alter, and use a corporate seal.

Second. To have perpetual succession from the date of enactment hereof, unless it is sooner dissolved by an act of Congress.

Third. To make contracts; to purchase, lease, and hold or dispose of such real estate or personal property as may be necessary or convenient for the transaction of its business.

Fourth. To sue and be sued, complain and defend in any court of competent jurisdiction.

Fifth. To appoint, employ, and fix the compensation of such officers, employees, attorneys, and agents as shall be necessary for the transaction of the business of the corporation, without regard to the provisions of other laws applicable to the employment and compensation of officers or employees of the United States, to define their authority and duties, to require bonds of them and fix the penalty thereof and to dismiss them at pleasure. Nothing in this or any other act shall be construed to prevent the appointment and compensation as a director, officer, or employee of the corporation of any officer or employee of the United States in any board, commission, independent establishment, or executive department thereof.

Sixth. To prescribe, amend, and repeal by its board of directors by-laws and rules and regulations not inconsistent with law governing the manner in which

its general business may be conducted and the privileges granted to it by law may be exercised and enjoyed.

Seventh. To exercise such incidental powers as shall be reasonably necessary to carry out the powers so granted.

(e) The board of directors of the corporation shall determine and prescribe the manner in which its obligations shall be incurred and its expenses allowed and paid. The corporation shall be entitled to the free use of the United States mails in the same manner as the executive departments of the Government. The corporation with the consent of any Federal reserve bank or of any board, commission, independent establishment, or executive department of the Government, including any field service thereof, may avail itself of the use of information, services, and facilities thereof in carrying out the provisions of this act.

(f) Upon the application of the receiver of any member bank, the corporation may in its discretion purchase the assets of such bank, in whole or in part, or make loans to the receiver on the security of such assets or any portion thereof, on such terms and conditions as shall be agreed upon between the corporation and the receiver, subject to the approval of (1) the Comptroller of the Currency in the case of any national bank, or (2) the person or agency designated by State law in the case of any State bank; except that, in no case shall the corporation make any loan or purchase any assets in an amount which in the opinion of the corporation shall not fully protect such corporation and no such loan or purchase shall be made in the case of State member banks unless expressly authorized by the law of the State in which the bank is located. Receivers of national banks are hereby authorized and empowered with the approval of the Comptroller of the Currency to borrow on, or sell, assets of banks of which they are receivers, and the proceeds of every such sale or loan shall be utilized for the same purposes and in the same manner as other funds realized from the liquidation of the assets of such banks. The Comptroller of the Currency may, in his discretion, pay dividends on proved claims at any time after the expiration of the period of advertisement made pursuant to section 5235 of the Revised Statutes, and no liability shall attach to the Comptroller of the Currency or to the receiver of any national bank by reason of any such payment for failure to pay dividends to a claimant whose claim is not proved at the time of any such payment. If the amount realized from any assets acquired by the corporation under the provisions of this section exceeds the sum paid therefor or loaned thereon, the corporation shall make an additional payment to the receiver of the bank equal to the amount of such excess, if any, after deducting the expenses of liquidating such assets and an amount equal to interest at the rate of 6 per cent per annum. All loans made by the corporation to receivers shall bear interest at the rate of 6 per cent per annum.

(g) Money of the corporation not otherwise employed shall be invested in securities of the Government of the United States, except that for temporary periods, in the discretion of the board of directors, funds of the corporation may be deposited subject to check in any Federal reserve bank or with the Treasurer of the United States. When designated for that purpose by the Secretary of the Treasury, the corporation shall be a depository of public moneys, except receipts from customs, under such regulations as may be prescribed by the said Secretary, and may also be employed as a financial agent of the Government. It shall perform all such reasonable duties as depository of public moneys and financial agent of the Government as may be required of it.

(h) The corporation is authorized and empowered to issue and to have outstanding at any one time in an amount aggregating not more than twice the amount of its capital, notes, debentures, bonds, or other such obligations, to be redeemable at the option of the corporation before maturity in such manner as may be stipulated in such obligations, to bear such rate or rates of interest, and to mature at such time or times as may be determined by the corporation: *Provided*, That the corporation may sell on a discount basis short-term obligations payable at maturity without interest. Obligations of the corporation may be secured by assets of the corporation in such manner as shall be prescribed by the board of directors. Such obligations may be offered for sale at such price or prices as the corporation may determine. The said obligations shall be fully and unconditionally guaranteed both as to interest and principal by the United States and such guaranty shall be expressed on the face thereof. In the event that the corporation shall be unable

to pay upon demand, when due, the principal of or interest on notes, debentures, bonds, or other such obligations issued by it, the Secretary of the Treasury shall pay the amount thereof, which is hereby authorized to be appropriated, out of any moneys in the Treasury not otherwise appropriated, and thereupon to the extent of the amounts so paid the Secretary of the Treasury shall succeed to all the rights of the holders of such notes, debentures, bonds, or other such obligations.

(i) All obligations issued by the corporation shall be exempt, both as to principal and interest, from all taxation (except estate or inheritance taxes) now or hereafter imposed by the United States, by any Territory, dependency or possession thereof, or by any State, county, municipality, or local taxing authority. The corporation, including its franchise, its capital, reserves, and surplus, and its income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority, except that any real property of the corporation shall be subject to State, county, municipal, or local taxation to the same extent according to its value as other real property is taxed.

(j) In order that the corporation may be supplied with such forms of obligations as it may need for issuance under this act, the Secretary of the Treasury is authorized to prepare such forms as shall be suitable and approved by the corporation, to be held in the Treasury subject to delivery, upon order of the corporation. The engraved plates, dies, bed pieces, and other material executed in connection therewith shall remain in the custody of the Secretary of the Treasury. The corporation shall reimburse the Secretary of the Treasury for any expenses incurred in the preparation, custody, and delivery of such obligations.

(k) The corporation shall annually make a report of its operations to the Congress as soon as practicable after the 1st day of January in each year.

(l) Whoever, for the purpose of obtaining any loan from the corporation, or any extension or renewal thereof, or the acceptance, release, or substitution of security therefor, or for the purpose of inducing the corporation to purchase any assets, or for the purpose of influencing in any way the action of the corporation under this act, makes any statement, knowing it to be false, or willfully overvalues any security, shall be punished by a fine of not more than \$5,000, or by imprisonment for not more than two years, or both.

(m) Whoever (1) falsely makes, forges, or counterfeits any obligation or coupon, in imitation of or purporting to be an obligation or coupon, issued by the corporation, or (2) passes, utters, or publishes, or attempts to pass, utter, or publish, any false, forged or counterfeit obligation or coupon, purporting to have been issued by the corporation, knowing the same to be false, forged or counterfeited, or (3) falsely alters any obligation, or coupon, issued or purporting to have been issued by the corporation, or (4) passes, utters, or publishes or attempts to pass, utter, or publish as true, any falsely altered or spurious obligation or coupon, issued or purporting to have been issued by the corporation, knowing the same to be falsely altered or spurious, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

(n) Whoever, being connected in any capacity with the corporation, (1) embezzles, abstracts, purloins, or willfully misapplies any moneys, funds, securities, or other things of value, whether belonging to it or pledged, or otherwise entrusted to it, or (2) with intent to defraud the corporation or any other body, politic or corporate, or any individual, or to deceive any officer, auditor, or examiner of the corporation, makes any false entry in any book, report, or statement of or to the corporation, or without being duly authorized draws any order or issues, puts forth or assigns any note, debenture, bond, or other such obligation, or draft, bill of exchange, mortgage, judgment, or decree thereof, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

(o) No individual, association, partnership, or corporation shall use the words "Federal Liquidating Corporation," or a combination of these three words, as the name or a part thereof under which he or it shall do business. Every individual, partnership, association, or corporation violating this subdivision shall be punished by a fine of not exceeding \$1,000, or by imprisonment not exceeding one year, or both.

(p) The provisions of sections 112, 113, 114, 115, 116, and 117 of the Criminal Code of the United States (U. S. C., title 18, ch. 5, secs. 202 to 207, inclusive),

insofar as applicable, are extended to apply to contracts or agreements with the corporation under this act, which for the purposes hereof shall be held to include loans, advances, extensions and renewals thereof, and acceptances, releases, and substitutions of security therefor, purchases or sales of assets, and all contracts and agreements pertaining to the same.

(q) The Secret Service Division of the Treasury Department is authorized to detect, arrest, and deliver into the custody of the United States marshal having jurisdiction any person committing any of the offenses punishable under this section.

Senator GLASS. Governor, was it your judgment that it was all right for the banks to contribute four times as much to the National Credit Corporation?

Mr. MEYER. That was a temporary contribution, Senator Glass. It was only intended to be so, and I think it will prove to be so.

Senator GLASS. This contribution is a single contribution and only a contribution.

Mr. MEYER. Yes; but I think it is expected that the National Credit Corporation will be able to return all of its capital.

Senator GLASS. The whole proposition is whether this is a propitious time to require the banks of the country to contribute four times as much to the National Credit Corporation as to this corporation.

Mr. MEYER. All banks did not do it, only about half of them.

Senator GLASS. And they were coerced into doing it?

Mr. MEYER. Some of them, perhaps.

Senator GLASS. We had testimony the other day that they only did it then after they were assured by high authority that the Government through the taxpayers was going to take it over.

Mr. MEYER. Well, I think that the \$100,000,000 capital for the corporation, which is less than you suggested in the bill should come from the Government, and that, with \$200,000,000 borrowing capacity, would enable the corporation to take care of the need for advances to facilitate payments to depositors of closed banks.

Senator GLASS. Has the Government ever contributed a dollar to the maintenance of the Federal reserve system?

Mr. MEYER. I know they have not in the last year and a half.

Senator GLASS. And you know they have never done it, either.

Mr. MEYER. Well, I will say that I think they have not, but you understand I can not speak on that from personal knowledge.

Senator GLASS. And why should it ever do it? It is not a Government institution.

Mr. MEYER. No.

Senator GLASS. The Government does not own one dollar of proprietary interest in the Federal reserve system, and I for one have been intent on keeping it that way. I don't think the Government should have anything to do with it except by way of supervisory control.

Senator FLETCHER. How about nonmember banks being taken care of?

Mr. MEYER. There are a good many States which do not authorize receivers of closed banks to borrow. Some of the States are amending their laws, but some are not. Virginia amended its law.

Senator FLETCHER. The point I am making is, that the Reconstruction Finance Corporation itself is a temporary corporation.

Mr. MEYER. Yes.

Senator FLETCHER. Whereas we are trying to write here a permanent law.

Mr. MEYER. Yes.

Senator FLETCHER. So the Reconstruction Finance Corporation can not take care of the needs of these nonmember banks very well.

Mr. MEYER. Yes, but—

Senator GLASS (interposing). The provision in this bill with respect to nonmember banks is a temporary arrangement. I must confess that I had no particular partiality for it, and I have been trying to ascertain from the Reconstruction Finance Corporation within the last three or four days whether or not it thinks there is any need for that temporary relief. In other words, whether the \$200,000,000 already appropriated is not sufficient to meet that issue.

Mr. MEYER. It is hard to answer that question. If some States which have no laws authorizing borrowings by receivers, should amend their laws and authorize them, I think there might be a considerable volume of applications for this purpose. But in the immediate present there is not, because most States have no laws which permit borrowings by receivers of State banks.

Senator GLASS. This provision would expire by limitation before many States could take advantage of it.

Mr. MEYER. It depends on how long that corporation functions. If for only one year, which I hope may be the case, that would be so, but its life might be extended.

Senator GLASS. This particular provision expires in two years.

Mr. MEYER. Yes, sir.

Senator WALCOTT. Governor Meyer, would your proposed amendment make this an emergency measure or a permanent measure?

Mr. MEYER. Permanent.

Senator WALCOTT. The same as this bill?

Mr. MEYER. Yes; but for member banks.

Senator WALCOTT. For member banks only?

Mr. MEYER. Yes, sir.

Senator GLASS. I should like to recapture from the Government the whole of the \$147,000,000 it has taken over from the Federal reserve bank earnings and to which it was never entitled in my judgment.

Mr. MEYER. Well, this would recapture \$100,000,000 as it is proposed here.

Senator GLASS. But it does not appear in the form of a recapture.

Mr. MEYER. I have the feeling, Senator Glass, that to take a large part of the surplus of the Federal reserve banks and put it in the corporation would be a mistake.

Senator GLASS. The Federal reserve banks have more than 100 per cent greater surplus than they asked the Congress to give them.

Mr. MEYER. Well, it is a great element of strength in the banks, and adds to the confidence of the people in the Federal reserve system. The surplus of any bank is as important to its capital structure as its capital. The mere fact that it is called surplus does not mean that it can be taken out without detriment.

Senator GLASS. We are not divorcing it. We are putting it to the use of the member banks of the system.

Mr. MEYER. Yes. In an acute situation when the real test of confidence in strength develops the large surplus as well as the capi-

tal of the Federal reserve system is a very important element, and it never was more so than it was within the past year, and, if that surplus had been invested, even well invested, in slow assets of closed banks, I should say it would not have been as much in the public interest as it was to keep it in reasonably liquid form.

Senator GLASS. And instead of that it was invested largely in slow assets of foreign banks in foreign countries.

Mr. MEYER. Not very extensively.

Senator GLASS. But quite extensively.

Mr. MEYER. These advances have been repaid in large part.

Senator GLASS. Nevertheless, the investment was very extensive.

Mr. MEYER. It was not very prolonged. That not all of it was slow has been proven by the fact that a considerable part has already been retired.

Senator GLASS. But it never ought to have been done at all.

Mr. MEYER. Shall I now proceed, Mr. Chairman?

The CHAIRMAN. Proceed with your statement.

Mr. MEYER. I will take up section 11: Section 11 imposes a discriminatory rate against member-bank collateral notes. It also prescribes limitations on the use of such notes by banks that may be making loans on stock-exchange collateral. It is believed that the purposes of this section are accomplished by the proposed revision of section 3 and that no further limitations along this line are desirable. The theory underlying this section, namely, that there is a more direct connection between member-bank collateral notes and the use of reserve credit for speculative activity than between other borrowings and this activity is unfounded. Member banks borrow on 15-day notes, because of the greater convenience both to them and to the Federal reserve bank; and, if this form of borrowing were prohibited or made more expensive, they would merely substitute the procedure of rediscounting eligible paper without any change in the use of the proceeds. For these reasons, it is believed that this section would make the operation of the Federal reserve banks less efficient and more expensive.

The recommendation has been made by the Federal Reserve Board in its annual reports for several years that the maturity for which advances may be made to member banks on their promissory notes secured by paper which is eligible for discount be increased from 15 to 90 days. Such an amendment would be especially helpful to country banks, and it is recommended that the following be substituted for section 11 of the bill:

Sec. 11. The seventh paragraph of section 13 of the Federal reserve act, as amended, is amended and reenacted to read as follows:

Any Federal reserve bank may make advances for periods not exceeding 15 days to its member banks on their promissory notes secured by the deposit or pledge of bonds, notes, certificates of indebtedness or treasury bills of the United States; and any Federal reserve bank may make advances for periods not exceeding 90 days to its member banks on their promissory notes secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this act. All such advances shall be made at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board.

Section 12: Section 12 deals with relations of Federal reserve banks with foreign banks. It is recommended that the words "subject to the powers conveyed to and bestowed upon the Federal open

market committee by section 12A of this act" be omitted. From the middle of line 18 on page 26 through the word "writing" in line 11 on page 27, the section is acceptable, but the omission of the words "and control" in line 19 on page 26 is suggested, in order to preserve the distinction between supervision and operation.

It is recommended, therefore, that section 12 of the bill be amended as follows:

(1) Strike out the following language in lines 16, 17, and 18 on page 26:

(g) Subject to the powers conveyed to and bestowed upon the Federal open market committee by Section 12A of this Act;

(2) Strike out the words "and control" in line 19 on page 26; and

(3) On page 27, line 11, insert a period after the word "writing" and strike out everything in line 11 after that word and all of lines 12, 13, 14, and 15.

Senator GLASS. What you read back there furnishes more fuel to the fire, doesn't it?

Mr. MEYER. I think not, Senator Glass. I find in country districts of the Federal reserve banks a very great desire to use bills payable as a matter of convenience. It is not confined to large cities or large money markets.

Senator GLASS. But it is principally used there, isn't it?

Mr. MEYER. Of course those banks are larger and they use everything more; and abuse everything more sometimes. I think you will agree with me on that, won't you?

Senator GLASS. Yes, but if I could get you to agree with me I would feel more comfortable. [Laughter in the room.]

Mr. MEYER. Well, Senator Glass, in reading a comment of this kind I think it is well to bear in mind that it consists of a list of matters where there are differences of opinion and suggestions for amendments. It does not, of course, undertake to recite a large number of matters and the many points on which the board is in thorough agreement with you and in sympathy with your point of view. It appears from reading a document of this kind that it enumerates only the differences, because that is all there is any use in enumerating, and therefore it appears perhaps to be nothing but disagreement. However, as stated in the covering letter which I read, the board is in sympathy with the general purpose and point of view of the bill; and I think you will agree with me that substantially there is a great deal in common between your point of view and the point of view of the board.

Senator GLASS. Oh, yes. I think the most of the changes are changes of phraseology.

Mr. MEYER. A good many of them at least.

Senator GLASS. Let me ask you this: The bank now has unrestrained power, subject to the review and determination of the Federal Reserve Board, to make the rate anything it chooses on 15-day paper, doesn't it?

Mr. MEYER. Yes.

Senator GLASS. It has great power, hasn't it?

Mr. MEYER. Yes.

Senator GLASS. Why do you suppose it was put in there?

Mr. MEYER. To be used in case of need.

Senator GLASS. And perhaps never to be used. There was no need for it in 1928 and 1929, was there?

Mr. MEYER. Senator Glass, I would not say, for I can not testify on that.

Senator GLASS. Oh, now! Well, you know what happened at least in 1928 and 1929.

Mr. MEYER. I am not a good witness on 1928 and 1929. I should like to be able to testify on 1928 and 1929; but, I prefer to refrain from posing as knowing very much about operations in that year because I know no more than anyone else on the outside.

Senator GLASS. Oh, well, now!

Mr. MEYER. I am not afraid to answer your questions, as you know, Senator Glass, and I should like to do it; but I do not like to testify on things I do not know about.

Senator GLASS. Well, Governor Meyer, you are a philosopher and I am a layman. Let me ask you a direct question if you can understand it. [Laughter.] Should we eliminate the 1 per cent penalty and leave the board free to impose any penalty it might please, would you then object to the balance of the section? Don't you think a Federal reserve bank and the board should have the right to warn a stock-gambling bank, which is using the facilities of the Federal reserve—well, I did not ask that question of your counsel.

Mr. MEYER. I have already answered it, because you will find that we are trying in section 3 to cover exactly what you had in mind, in the amendment to that section that we propose.

Senator GLASS. Exactly. But I think you come far from doing it. That is what I am asking you now. If you will eliminate the minimum penalty and leave the board and the bank free to impose any penalty it may please, which it never has done, is there any further objection to that provision of the bill?

Mr. MEYER. Yes; because I think it violates the general principle of what I think is good administration. That is, to place the matter in the hands of administrative officers and then hold them responsible rather than to try to legislate in the matter of administration.

Senator GLASS. We did that, and they told you to go to a warmer place than this room supplies.

Mr. MEYER. They did not tell me anything of the kind, Senator. I was not there.

Senator GLASS. Oh, I know that you were not there.

Mr. MEYER. I have the feeling that the Federal reserve is a very young system, with no great tradition and history behind it. The banking system in this country as established in the last 20 years has not the background of history and tradition such as has guided other banking systems, where they made just as bad and even worse mistakes than have been made in this system, as is shown by their history. If you will read the history of the Bank of England, which is now more governed by tradition than by law, you will find numerous mistakes that they made, as great as any you can well imagine.

Senator GLASS. Oh, Governor Meyer, I never thought you would play the baby act in extenuation for the affront put upon the Federal reserve banks and the Federal Reserve Board in 1929.

Mr. MEYER. I am not doing that, Senator Glass. And I again feel that I ought not to be asked to be responsible for the conduct of officers in that period.

Senator GLASS. Oh, well, I would say if you remain as Governor of the Federal Reserve Board interminably we will not have a repetition of that maybe, but that is not to be supposed.

Mr. MEYER. I am glad that you feel that way, Senator Glass. I do not want to pride myself on being able to do better than other men, but we do learn by experience and I hope are bringing about better practices. The administration of any system will depend upon the men the Government is able to command for public service. The problem is to get men to discharge the responsibilities that you lay upon them and that you properly expect from them when you enact a law. You can not, in my opinion, enact into administration things that you can only get from wisdom, and above all things, moral courage, the lack of which is what you were complaining of as I see it. How you can legislate moral courage I have not been able to see.

Senator GLASS. We have not tried to do that.

Mr. MEYER. That is what it takes.

Senator GLASS. We have simply tried to avert a tradition that I do not want to see persist. If the tradition of 1928 and 1929 is going to be the guide of the bank and the board it would be a pretty bad situation.

Mr. MEYER. There are many things to consider. The system grew up in the war period, Senator Glass; it struggled with the post-war conditions and abnormal situations until the middle twenties, and almost before the war and the post-war crises had ended it was in the inflation period. I think it is quite easy to see the mistakes, but it is also possible to understand why those mistakes were made, and while I do not think they ought to be condoned, I think we ought to try to understand what produced them and avoid them in the future. I do not think you can insure sound administration and courageous administration by legislation alone.

Senator GLASS. You think your proposed amendment to section 3 will accomplish the same purpose as section 11?

Mr. MEYER. I think it does.

Senator GLASS. It is just a little more polite?

Mr. MEYER. Yes; I think it is a little better, and the board does, and it is the unanimous opinion of the board. I am speaking on that for the board.

Now may I read section 13?

The CHAIRMAN. Yes. You may go ahead.

Mr. MEYER. Section 13: The principal feature of this section is that it discontinues the distinction between time deposits and demand deposits in so far as reserve requirements are concerned. The distinction between these two types of deposits has led to many abuses and has been a factor in making possible a growth of bank credit without a corresponding growth in reserves. The proposal which would raise the requirements on time deposits to the level of those on demand deposits would increase reserve requirements by \$132,000,000 a year for five years with an ultimate increase of \$660,000,000.

Without proceeding to read that through I will say that the idea, of course, is one with which the members of the committee are thor-

oughly familiar. The board feels justified in recommending the plan of—

Senator GLASS. (interposing). Your velocity system.

Mr. MEYER. The velocity system, and it has confidence that it will serve the public interest better than the existing reserve law and regulations, and better than the plan proposed in the report of the committee.

Senator GLASS. I agree with the board; but I do not think the board nor I nor anybody else can convince the banks of that fact.

Mr. MEYER. There were several witnesses, and I have not read the testimony of many of them, but I think there were a good many who testified in favor of the report of the committee on bank reserves of the Federal reserve system. It has been thoroughly investigated by many outside the committee that evolved the plan, and I will add that it has been favorably commented on by foreign experts. Recently I read an article favoring it, in the *Economic Journal* of London, by a man who is an expert on monetary matters.

Senator GLASS. And he has been as often mistaken as anybody else in some matters. And New York banks bitterly criticized it.

Mr. MEYER. Well, Senator Glass, sometimes you consider that an argument in its favor and sometimes not.

Senator GLASS. Is that why you favor it—because they opposed it?

Mr. MEYER. No. I favor it because, after studying it, and not only studying the report itself, but studying the methods by which the committee arrived at the result, it seemed all right. The work of that committee represents a very careful scientific study and a conscientious effort to arrive at a plan of reserves which would work soundly and constructively. It would relax credit in depressions and require an increasing volume of reserves in an expansion period. They would have caught all these outside loans which were so disastrous in 1929 by this method. And they have convinced the board I think, as well as many outside students of the problem, of the soundness of their recommendation, by the thoroughness with which they have applied tests of the proposal to past conditions over a long period of years.

Senator GLASS. I did not dissent at all and the subcommittee generally did not dissent from the views you express now. But do you think now is the opportune time to introduce anything of a revolutionary nature into the banking business?

Mr. MEYER. This gives a six months' period for member banks to study it, and that ought to be all they need. If six months won't teach them to understand it then six years won't. From the financial point of view, I should say there is nothing to fear in it, and that it is not revolutionary. It does not radically change the aggregate amount of reserves required, and it is not a thing that needs to be feared.

Senator GLASS. Would you advocate either a maximum or a minimum or both?

Mr. MEYER. Well, there is a minimum. The minimum is 5 per cent for all classes of deposits. I want to express the greatest sympathy with your point of view about time deposits and the abuses that have developed in that connection, and the report of the committee is designed to do the same thing that you have in mind there.

Senator GLASS. I am glad to get a little sympathy.

Senator BULKLEY. Do I understand that the recommendation of the board is the same as the report of the technical committee we had several months ago?

Mr. MEYER. I have not compared the two. There are some cases for which it seemed desirable to make special provision as suggested in this draft, in addition to the suggestions made in the report, for instance, where banks have a very heavy turnover.

Senator BULKLEY. Is that the exception, for pay rolls and dividends?

Mr. MEYER. I think that is covered, and one or two other forms of exceptions.

Senator BULKLEY. And you do recommend those exceptions?

Mr. MEYER. Yes; to the extent provided for in the proposed substitute for section 13 of the bill.

Senator WALCOTT. Do you include the maximum as well as the minimum provision?

Mr. MEYER. I think the maximum is 15 per cent.

Senator BULKLEY. Do you think that maximum would still be necessary if you make an exception for disbursements?

Mr. MEYER. I think so. I see no harm in it. A reserve of 15 per cent of gross deposits would be enough.

Senator WALCOTT. If the committee should use that would you have it active a little later?

Mr. MEYER. At the end of six months, as suggested in the proposed amendment. I have heard no criticism of the plan proposed by the committee on reserves. The only feeling I have perhaps is that we can not tell how it will work until it is put into effect. We tried to apply every possible test, and particularly the committee studied how it might be evaded, if at all, so that banks would be able to get by with less reserves than intended and than would be sound and safe. There has been no great difficulty or objection found in our experience which would justify our being afraid to recommend it.

And now I wish to read you the remainder of the memorandum in regard to section 13 of the bill:

Unless there were a contraction in the amount of member bank deposits, this increase would result in an addition of about \$230,000,000 to the gold requirements of the Federal reserve banks. It would be an influence in the direction of credit contraction without regard to the course of business and credit and would be particularly undesirable at this time. Furthermore, the increase would fall heaviest on banks outside of the principal financial centers, which have been discriminated against under the existing reserve requirements both because, owing to their distance from the cash facilities of the Federal reserve bank, they are required to carry relatively large amounts of cash in vault, which under existing law does not count as reserve, and because they are not in a position to take advantage of deductions in determining net deposits.

The proposal, therefore, would both increase the burden of reserves and increase the inequalities in their present distribution.

Any thorough-going revision of section 19 of the Federal reserve act should base required reserves, in so far as practicable, upon the activity of the business handled through each bank, rather than on an arbitrary classification of banks according to location. A proposal submitted in the report of the committee on bank reserves of the Federal reserve system embodies a method of calculating reserves which is believed to be sound in principle and which would make fluctuations in the volume of required reserves exert an influence in the direction of sound credit conditions and would also eliminate many inequitable and unfair features of the present law.

There is submitted a proposed substitute for section 13 of the bill which incorporates the proposals of the committee on bank reserves of the Federal reserve system with slight modifications.

Section 13 includes two subjects not directly related to bank reserves and not covered in the report of the reserve committee, namely, a prohibition against brokers' loans for the account of others and a provision subjecting the market for Federal funds to regulation by the Federal Reserve Board.

The purpose sought to be accomplished by paragraph (d) is desirable, but it is believed that the language used is too far reaching. It is suggested that the paragraph be changed so as to prohibit a member bank from acting as a medium or agent of a nonbanking corporation or individual in making loans on the security of stocks, bonds, and other investment securities to brokers or dealers in such securities. This suggestion is incorporated in paragraph (n) of the proposed revision of section 13 of the bill. It is not thought that a provision prohibiting a member bank from making loans to any corporation or individual if the proceeds of such transaction are to be used directly or indirectly for the purpose of making loans protected by collateral security in favor of any investment banker, broker, or member of any stock exchange or any dealer in securities, would be enforceable as it is impossible to follow the proceeds of loans once they have been granted.

Paragraphs (f) and (g) of the bill seek to control the market for Federal funds by placing limitations on the use of balances standing to the credit of member banks upon the books of the Federal reserve banks. It is not believed that regulation of the market for Federal funds by law is desirable. It is better to have these liquid funds move freely where they are most needed than to have them thrown on the call market. The Federal reserve banks keep in close touch with transactions in Federal funds and a ruling of the Federal Reserve Board now requires member banks to report purchases of Federal funds as borrowed money.

The proposed substitute for section 13 of the bill is as follows:

"Sec. 13. Section 19 of the Federal reserve act (U. S. C., title 12, sec. 461-466, incl., and sec. 374), as amended, is further amended and reenacted to read as follows:

"RESERVES OF MEMBER BANKS

"Sec. 19. (a) Each member bank shall establish and maintain reserves equal to five per centum of the amount of its net deposits, plus fifty per centum of the amount of its average daily debits to deposit accounts: *Provided*, That any member bank, at its option for any period not less than 90 days, may omit any specific deposit account or accounts from such computation of its reserve requirements if such account or accounts are reported separately to the Federal reserve bank and if a reserve of 50 per centum is maintained against such account or accounts: *Provided, however*, That in no event shall the aggregate reserves required to be maintained by any member bank exceed 15 per centum of its gross deposits.

"(b) Each member bank located in the vicinity of a Federal reserve bank or branch thereof shall maintain not less than four-fifths of its total required reserves in the form of a reserve balance on deposit with the Federal reserve bank and every other member bank shall maintain not less than two-fifths of its total required reserves in the form of a reserve balance on deposit with the Federal reserve bank. The remainder of the total required reserves of each member bank, over and above the amount required to be maintained in the form of a reserve balance on deposit with the Federal reserve bank, may, at the option of such member bank, consist of a reserve balance on deposit with the Federal reserve bank, or of cash owned by such member bank either in its actual possession or in transit between such member bank and the Federal reserve bank: *Provided*, That when, in its judgment the public interest so requires, the Federal Reserve Board may limit to an amount less than that permitted hereunder the amount of cash which any member bank or banks may count as reserve: *Provided, however*, That, in prescribing such limitations, the Federal Reserve Board shall be guided by the general principle that member banks should be permitted to count as reserve, within the limitations of this section, as much cash as they reasonably need in view of the character of their business and their degree of accessibility to the currency facilities of the Federal reserve banks.

"(c) The term "gross deposits," within the meaning of this section, shall include all deposit liabilities of any member bank whether or not immediately

available for withdrawal by the depositor, all liabilities for certified checks, cashiers', treasurers', and other officers' checks, cash letters of credit, travelers' checks, and all other similar liabilities, as further defined and specified by the Federal Reserve Board: *Provided, however*, That, in computing the amount of "gross deposits" (1) amounts shown on the books of any member bank as liabilities of such bank payable to a branch of such bank located in a foreign country or in a dependency or possession of the United States, and (2) liabilities payable only at such a branch, shall be treated as though said liabilities were due to or payable at a nonmember bank.

"(d) The term "net deposits," as used in this section, shall mean the amount of the gross deposits of any member bank, as above defined and as further defined by the Federal Reserve Board, minus the sum of (1) all balances due to such member bank from other member banks and their branches in the United States and (2) checks and other cash items in process of collection which are payable immediately upon presentation in the United States, within the meaning of these terms as further defined by the Federal Reserve Board.

"(e) The term "average daily debits to deposit accounts," as used in this section, shall mean the average daily amount of checks, drafts, and other items debited or charged by any member bank to any and all accounts included in gross deposits as above defined and as further defined by the Federal Reserve Board, except charges resulting from the payment of certified checks and cashiers', treasurers', and other officers' checks.

"(f) The term "cash" within the meaning of this section, shall include all kinds of currency and coin issued or coined under authority of the laws of the United States.

"(g) The term "reserve balances," as used in this section, shall mean a member bank's actual net balance on the books of the Federal reserve bank representing funds available for reserve purposes under regulations prescribed by the Federal Reserve Board.

"(h) The term "vicinity of a Federal reserve bank or branch thereof," as used in this section, shall mean the city in which a Federal reserve bank or branch thereof is located, until such term is otherwise defined by the Federal Reserve Board: *Provided*, That, with respect to each Federal reserve bank and each branch thereof, the Federal Reserve Board, from time to time, in its discretion, may either (1) define a specific geographic area as comprising the vicinity of such Federal reserve bank or branch thereof, within the meaning of this section, or (2) compile a list of member banks which shall be deemed to be located in the vicinity of such Federal reserve bank or branch thereof, within the meaning of this section, and add banks to, or remove banks from, such list, from time to time: *Provided, however*, That, in defining such areas and compiling such lists, the Federal Reserve Board shall be guided by the general principle indicated in subsection (b) hereof.

"(i) With respect to each member bank, the term "Federal reserve bank," as used in this section, shall mean the Federal reserve bank of the district in which such member bank is located.

"(j) The Federal Reserve Board is authorized and empowered to prescribe regulations defining further the various terms used in this act, fixing periods over which reserve requirements and actual reserves may be averaged, determining the methods by which reserve requirements and actual reserves shall be computed, and prescribing penalties for deficiencies in reserves. Such regulations and all other regulations of the Federal Reserve Board shall have the force and effect of law and the courts shall take judicial notice of them.

"(k) Subject to such regulations and penalties as may be prescribed by the Federal Reserve Board, any member bank may draw against or otherwise utilize its reserves for the purpose of meeting existing liabilities: *Provided, however*, That, whenever the reserves of any member bank have been continuously deficient for fourteen consecutive calendar days, the Federal reserve agent or assistant Federal reserve agent of the district in which such member bank is located shall send to each director of such bank, by registered mail, a letter advising him of such deficiency and calling attention to the provisions of this subsection; and each director of such bank who after receipt of such a letter, assents to or acquiesces in the making of additional loans or investments by such bank before the reserves of such bank shall have been restored to the amount required by this section, shall be held liable in his personal or individual capacity for any and all losses sustained by such bank on any such loans or investments.

"(l) All penalties for deficiencies in reserves incurred under regulations prescribed by the Federal Reserve Board pursuant to the provisions of this Act shall be paid to the Federal reserve bank by the member bank against which they are assessed.

"(m) No member bank shall keep on deposit with any State bank or trust company which is not a member bank a sum in excess of ten per centum of its own paid-up capital and surplus. No member bank shall act as the medium or agent of a nonmember bank in applying for or receiving discounts from a Federal reserve bank under the provisions of this act, except by permission of the Federal Reserve Board.

"(n) No member bank shall act as the medium or agent of any nonbanking corporation, partnership, association, business trust or individual in making loans on the security of stocks, bonds, and other investment securities to brokers or dealers in stocks, bonds, and other investment securities. Every violation of this provision by any member bank shall be punishable by a fine of not more than \$100 per day during the continuance of such violation; and such fine may be collected, by suit or otherwise, by the Federal reserve bank of the district in which such member bank is located.

"(o) National banks or banks organized under local laws, located in Alaska or in a dependency or insular possession or any part of the United States outside the continental United States, may remain nonmember banks, and shall in that event maintain reserves and comply with all the conditions now provided by law regulating them; or said banks may, with the consent of the Federal Reserve Board, become member banks of any one of the Federal reserve districts, and shall in that event take stock, maintain reserves, and be subject to all the other provisions of this act.

"(p) All acts or parts of acts in conflict with this section are hereby repealed only in so far as they are in conflict with the provisions of this section."

"There are hereby repealed the provisions of section 7 of the first Liberty bond act, approved April 24, 1917; section 8 of the second Liberty bond act, approved September 24, 1917, and section 8 of the third Liberty bond act, approved April 4, 1918 (U. S. C., title 31, sec. 771), which read as follows:

"That the provisions of section fifty-one hundred and ninety-one of the Revised Statutes, as amended by the Federal reserve act, and the amendments thereof, with reference to the reserves required to be kept by national banking associations and other member banks of the Federal reserve system, shall not apply to deposits of public moneys by the United States in designated depositories."

"This section shall become effective on the first day of the seventh calendar month following the enactment of this act."

Mr. MEXER. As to section 14, it is suggested that there should be some limit put upon the amount a bank may invest in bank premises, and an amendment is suggested.

The first portion of this section down to line 4 on page 33 is existing law. The sentence in lines 4 to 8, inclusive, is new and would interfere greatly with the financing of real-estate transactions. When a time loan has been made there appears to be no warrant, in the absence of default, for revising the valuations on which the loan is based; and this provision, together with that in lines 4 to 9 on page 34, would require the real estate on which each such loan is based to be revalued at least five times each year. It could not reasonably be expected that real-estate loans would be made or applied for under such conditions.

The sentence in lines 17 to 20 on page 33 would classify as real-estate loans all unsecured loans whose eventual safety depends upon the value of real estate, thereby subjecting all such loans to all the limitations or restrictions in this section. This would produce confusion and uncertainty in a large volume of loans and would interfere with the extension of adequate credit, particularly in the agricultural sections of the country.

The remaining amendments in this section make what appear to be unnecessary changes in the proportion of the real-estate loans permitted and propose, without segregation, to give time depositors a preferred claim on all real-estate loans and other assets of the bank acquired under this section. Such a provision would be difficult to administer and would be unfair to the other depositors.

The sentence in lines 15 to 22 on page 34 is existing law and is inconsistent with section 24 of the bill, which will be discussed later.

It would seem desirable to limit the amount which banks may invest in bank premises, but it is suggested that this be accomplished directly instead of indirectly.

It is recommended, therefore, that section 14 of the bill be stricken out and that the following new section be substituted:

SEC. 14. The Federal reserve act, as amended, is amended by inserting between section 24 and section 25 thereof the following new section:

SEC. 24 (a). Except with the permission of the Comptroller of the Currency, no national bank, and except with the permission of the Federal Reserve Board, no State member bank, shall hereafter invest in bank premises or in the stock or obligations of, or in loans to, any corporation owning or holding its bank premises a sum exceeding the amount of the capital stock of such bank."

Referring to section 14 I think, gentlemen of the committee, it is fair to say that the board is not confident about the soundness of the idea of segregating assets for each class of deposits in the same bank. As a matter of fact, in the various States there are different laws and different conditions prevail. But I heard the superintendent of banks of one important State say that if a large commercial bank having time deposits on a considerable scale were to give notice or avail itself of the right to delay payment, he would close the bank on the ground that it created a preference in favor of demand depositors. So that segregation of securities for special classes of deposits is not necessarily sound.

Senator GLASS. You say the limitation on the use of time deposits is rather too great there?

Mr. MEYER. I did not catch that question.

Senator GLASS. I understand you to say that the limitation on loans on real estate was too rigid.

Mr. MEYER. Well, as to the matter of appraisals—

Senator GLASS (interposing). I am not talking about appraisals.

Mr. MEYER. Well, all unsecured loans which are in a measure based upon real estate should not be considered as real-estate loans.

Senator GLASS. I am talking about the restriction of real-estate loans to 15 per cent.

Mr. MEYER. That is not what I was discussing here.

The CHAIRMAN. You may proceed.

Senator WALCOTT. What is the nature of that amendment?

Senator GLASS. Not more than the total of the capital.

Mr. MEYER. I think that is enough.

Senator FLETCHER. It has been suggested by one witness that in the matter of investments in bank premises and unsecured loans whose eventual safety depends upon the value of real estate "may be counted" for the purposes of this section as real estate loans, instead of "shall be counted" as contained in that section of the bill.

The CHAIRMAN. He recommends that we change the word "shall" to the word "may."

Senator FLETCHER. Yes. In other words, instead of making it mandatory that it would be permissive.

Mr. MEYER. What section is that?

Senator FLETCHER. Section 14 of the bill, page 33, line 19.

Mr. MEYER. I do not believe it is the proper thing to incorporate that idea into law. Let me read it [reading]:

Investments in bank premises and unsecured loans whose eventual safety depends upon the value of real estate shall be counted for the purposes of this section as real-estate loans.

It is a matter of opinion and judgment. Any farmer who had an unencumbered farm might borrow money for farming operations and the banker would have the knowledge from his financial statement that, while he was borrowing to grow a crop, if he did not make a profit or if the crop failed, or there was a loss, his background of strength would be his ownership of the unencumbered land. I do not think that makes it a real-estate loan. I do not think it ought to be considered so. I do not think anybody ought to have the right to call that a real-estate loan.

Senator FLETCHER. You think we ought to strike that out entirely?

Mr. MEYER. That is what we recommend. As a matter of fact, the land values of the country are back of so much of the loans that if we started to get back to the land you would end up with almost every loan a real-estate loan.

The CHAIRMAN. You may continue, Governor Meyer.

Mr. MEYER. As to section 15: This section would make it necessary for member banks to dispose of a large amount of securities at this time which would be very unfortunate. Since it is aimed generally at investments in securities, it is believed that its purpose is covered sufficiently by the proposed substitute for section 3 of the bill.

Senator COUZENS. What portion of that section do you think would make banks dispose of their securities? I can not find any.

Senator GLASS. No; and the subcommittee could find nothing of the kind.

Mr. MEYER. But I think a large number of people have.

Senator COUZENS. But I can not find it.

Senator GLASS. That was a part of the curriculum, Governor Meyer. [Laughter.]

Mr. MEYER. I will read from the bill [reading]:

But in no event shall the total amount of such investment securities of any one obligor or maker held by such association exceed 10 per centum of the total amount of such issue outstanding, nor shall the total amount of the securities so purchased and held for its own account at any time exceed 15 per centum of the amount of the capital stock of such association actually paid in and unimpaired and 25 per centum of its unimpaired surplus fund.

Senator COUZENS. This only applies to one obligor as you will notice on line 12. But perhaps the word "obligor" should be put lower down.

Mr. MEYER. But it says [reading]:

Nor shall the total amount of the securities so purchased and held.

Senator GLASS. But all in the case of one obligor.

Mr. MEYER. You are talking about the purchase of securities in this section?

Senator BULKLEY. It is the purchase of securities, but it means the purchase of a security of any one obligor.

Mr. MEYER. I see.

Senator COUZENS. There can not be any deflationary provision in that section if you understand it only applies to only one obligor.

Senator W^{ALCOTT}. How would that affect a total issue, for instance?

Senator C^{OUZENS}. I should say that a bank should not be permitted to take an entire issue. That was the intent of the section as I understand it.

Senator G^{LASS}. You will not permit a borrower engaged in commerce to borrow any more of a bank's funds than that, and why should you permit it in the case of real estate?

Mr. M^{EYER}. I have not considered this section with that meaning. I have considered it as relating to investments in the aggregate. I would have to study that further to say what it would mean. I would not like to express an opinion if that is the intent of the language.

Senator C^{OUZENS}. I think that is important, because the most of the public opinion that has been developed along the lines that this is a deflationary measure is based on that section.

Mr. M^{EYER}. That was one of them; yes.

Senator C^{OUZENS}. Is there any other section of the bill which is deflationary?

Mr. M^{EYER}. I think some of them might be called that. But that undoubtedly was one of them, and perhaps the most far-reaching.

Senator C^{OUZENS}. And so far as you can see that was the main one which caused the public to think that?

Mr. M^{EYER}. The language certainly lends itself to the interpretation put on it, because so many people have read it that way.

Senator G^{LASS}. The strange thing to me is that we have had to explain over and over again to every witness that that is not what is meant. But they have their lesson by rote and they just come in and give it to us.

Mr. M^{EYER}. Well, I got it from reading the bill.

Senator G^{LASS}. Oh, yes; I know that you did not have to go to night school.

Mr. M^{EYER}. I will now continue with section 15.

Senator W^{ALCOTT}. It seems to me we should not pass over that but ought to try to settle it. This is one of the most controversial points in the whole bill. Every witness has dwelt on that to great length. If that language needs clarifying, let us do it.

Senator G^{LASS}. Oh, we have indicated over and over again that we will do it, and we have told witness after witness what it means, and yet the very next witness comes along and makes the same statement.

Senator C^{OUZENS}. We have told the witnesses that the word "obligor" means what we have said.

Mr. M^{EYER}. Well, I did not draft the bill.

Senator W^{ALCOTT}. Will you suggest language to us?

Mr. M^{EYER}. If the committee desires a suggestion as to a draft to cover the intent as expressed by the committee we will be glad to make a suggestion.

Senator F^{LETCHER}. Do you comment on that in dealing with section 15?

Senator C^{OUZENS}. I think if you would put on line 15 after the word "securities" the words "of any one obligor," it would clarify it.

Senator G^{LASS}. That is what we have written into the bill.

Senator COUZENS. But perhaps that would clarify it.

Mr. MEYER. I will be glad to offer a suggestion in writing on it if you desire.

Senator GLASS. We would be glad to have you do it. You have here innumerable suggestions in writing.

Mr. MEYER. Well, it seems to be quite clear that it is not clear to the public.

Senator COUZENS. I think we left out a necessary word.

The CHAIRMAN. You may continue, Governor Meyer.

Mr. MEYER. Further, in regard to section 15: The clause commencing in line 19 on page 35 apparently is intended to enable national banks to compete more effectively with State banks. Its tendency would be to lower the standards of banking in the national banking system to the standard of the State banks, where more liberal powers are granted to State banks by State law.

The definition of investment securities which is contained in the law, as amended by the act of February 25, 1927, would be stricken out and apparently the comptroller would be given unlimited power to prescribe his own definition except that stocks could not be included. This modification is undesirable.

For the reason stated, it is recommended that this section be omitted entirely.

But with the other idea as to the intent, which you have discussed here, I should like to ask our counsel to make a suggestion as to a draft.

Section 16: This amendment is believed to be desirable; but it is recommended that it be strengthened and that a means of evasion be eliminated by striking out the exception in lines 17 to 21, inclusive, on page 37, which would permit the organization of national banks with a capital of \$25,000 in certain circumstances.

Section 17: The modification of the units in which bank stocks can be issued would create unnecessary complications; and it is recommended that all of section 17 be omitted, with the exception of the sentence in lines 17 to 23 on page 38, which should be made effective not less than three years after enactment.

As modified, section 17 would read as follows:

SEC. 17. Section 5139 of the Revised Statutes, as amended, is amended by adding at the end thereof a new paragraph reading as follows:

"After three years from the date of the enactment of this act no certificate representing the stock of any such association shall represent the stock of any other corporation, nor shall the ownership, sale or transfer of any certificate representing the stock of any such association be conditioned in any manner whatsoever upon the ownership, sale, or transfer of a certificate representing the stock of any other corporation."

Section 18: The first part of this section would prohibit any director, officer, or employee of any member bank from acting as a director, officer, or employee of certain other specified classes of business enterprises. It would be capable of easy evasion and would become ineffective in many cases. The latter part of the section would prohibit any member bank from clearing checks or doing the ordinary banking business of a correspondent for any of the types of business enterprises mentioned in this section. The language of the section is so broad that it would include banks within the classes of business enterprises to which the prohibitions of the section would apply. For example, all interlocking bank directorates now expressly

authorized by law or permitted under certain conditions would be prohibited, and one bank would be prohibited from acting as a correspondent of another bank. It is therefore recommended that this entire section be omitted.

It has been clearly demonstrated that affiliations between member banks and security companies have contributed to undesirable banking developments. There are, however, difficulties in the way of accomplishing a complete divorce of member banks from their affiliates arising from the fact that a law intended for that purpose is likely to be susceptible of evasion or else to apply to many cases to which it is not intended to apply. Therefore, the board is not prepared at this time to make a definite recommendation, but submits, for the consideration of the Committee on Banking and Currency, a substitute for section 18 which is designed to provide for the divorce of security affiliates from member banks after three years:

SEC. 18. From and after three years from the date of the enactment of this act, no member bank shall be affiliated in any manner described in section 2 (b) hereof with any corporation, association, business trust, or other similar organization engaged principally in the issue, flotation, underwriting, public sale, or distribution at wholesale or retail, of stocks, bonds, debentures, notes, or other securities.

For every violation of this section the member bank involved shall be subject to a penalty not exceeding \$1,000 per day for each day during which such violation continues. Such penalty may be assessed by the Federal Reserve Board, in its discretion, and, when so assessed, may be collected by the Federal reserve bank by suit or otherwise.

If any such violation shall continue for six calendar months after the member bank shall have been warned by the Federal Reserve Board to discontinue the same, (a) in the case of a national bank, all the rights, privileges and franchises granted to it under the national bank act may be forfeited in the manner prescribed in section 5239 of the Revised Statutes, or, (b) in the case of a State member bank, all of its rights and privileges of membership in the Federal reserve system may be forfeited in the manner prescribed in section 9 of the Federal reserve act.

It is fair to say that, while the board is in agreement on the views stated, there has been a good deal of discussion of the thought that the question of divorce of affiliates might perhaps be better deferred, instead of acting at this time to be effective three years from now, and in the meantime to get reports and make examinations and then enact a law later. However, the suggestion here was agreed upon as the best we could think of at the present time in the light of existing information, or I might say in the absence of full information on the subject. We do not feel, in the absence of more definite information, any too great confidence in any recommendation that we or anyone else could make. But this is a suggestion for your consideration, which was the best we could evolve in the board with the assistance of our experts.

If the bill is enacted into law and reports flow to the Federal Reserve Board from affiliates, and information is developed that would throw new light on it, I hope the board and the committee would feel free to exchange views in the light of the information obtained and the Congress could make any amendment that seemed necessary in the provision offered at the present time for affiliate separation.

Sections 19 and 20: It is recommended that section 19 of the bill be combined with section 20 in the manner hereinafter proposed: that the combined section be known as section 19; and that a new

section applicable to holding companies which own or control State member banks be substituted for section 20.

Under the definition of "affiliate" contained in section 2 and under the provisions of sections 6, 27, and 28 of the bill, if amended in accordance with the recommendations contained in this report, all holding companies which control member banks and all banks owned or controlled by such holding companies will be affiliates of such member banks and will be required to make reports and submit to examinations whenever deemed necessary or advisable by the Comptroller of the Currency, the Federal Reserve Board or examiners appointed by them; and, therefore, it is suggested that the provisions regarding examinations and condition reports of holding companies be omitted from this section and from the corresponding sections regarding holding companies which own or control State member banks.

It is also suggested that there be inserted in section 19 and in the proposed new section 20 certain additional provisions providing for the regulation and supervision of holding companies and requiring all eligible State banks controlled by them to be members of the Federal reserve system.

It is, therefore, recommended that section 19 of the bill be changed to read as follows:

Sec. 19. Section 5144 of the Revised Statutes, as amended, is amended to read as follows:

"Sec. 5144. In all elections of directors, and in deciding all questions at meetings of shareholders, each shareholder shall be entitled to one vote on each share of stock held by him, except that shares of its own stock held by any national bank as trustee shall not be voted, and shares owned or controlled by any affiliate, as defined by the banking act of 1932, or by any officer, director, employee, proxy, nominee, or representative or agent thereof, shall not be voted unless such affiliate shall have filed with the Comptroller of the Currency an agreement in such form as may be prescribed by him accepting, and agreeing to submit to and comply with, all of the provisions of this section, and such agreement shall not have been terminated. Shareholders may vote by proxies duly authorized in writing; but no officer, clerk, teller, or bookkeeper of such association shall act as proxy; and no shareholder whose liability is past due and unpaid shall be allowed to vote.

"Within a period of one year from the date of any such agreement, each nonmember State bank owned or controlled by such affiliate which is eligible for membership in the Federal reserve system shall apply for membership therein in the manner prescribed by, and subject to the terms of, section 9 of the Federal reserve act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal reserve system and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any such bank shall fail to become, or shall cease to be, a member of the Federal reserve system at any time while such agreement remains in effect, such affiliate shall divest itself of all stock ownership or other interest in, or control of, such bank.

"Except as otherwise provided herein, every such affiliate. (1) on January 1, 1934, and at all times thereafter while such agreement remains in effect, shall possess, free and clear of any lien, pledge or hypothecation of any nature, readily marketable assets other than bank stock, which shall not amount to less than 15 per centum of the aggregate par value of bank stocks held or owned by such affiliate, and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding, until its readily marketable assets other than bank stocks shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it; *Provided, however*, That, in computing the amount of readily marketable assets, other than bank stock, which any such affiliate is required to possess at any given time, credit shall be given to such affiliate for all contributions which it has made during the preceding three years to banks owned or controlled by it at the time such

computation is made. The term 'contribution,' as herein used, shall include all such gifts of money, assets or other things of value to any such bank, all such amounts paid for worthless or doubtful assets purchased from any such bank, and all such other similar amounts as the Comptroller of the Currency, in his discretion, may permit to be treated as contributions.

"If any such affiliate shall fail to comply with the provisions of this section or with the provisions of any agreement with the Comptroller of the Currency made pursuant thereto, the Comptroller, in his discretion, may terminate such agreement.

"Any officer, director, agent, or employee of any such affiliate, which has entered into an agreement with the Comptroller of the Currency in accordance with the provisions of this section, who shall make any false entry in any book, report or statement of such affiliate with intent in any case to injure or defraud such affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such affiliate or of any member bank, or the Comptroller of the Currency, or any agent or examiner appointed to examine the affairs of such affiliate, shall be deemed guilty of a misdemeanor and upon conviction thereof in any district court of the United States shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No national bank shall (1) make any loan on the stock of any affiliate which owns or controls such national bank directly or indirectly; (2) make any loan to any affiliate which owns or controls such national bank, directly or indirectly, on the security of any shares of stock of any corporation owned or controlled by such affiliate, or (3) be the purchaser or holder of the stock of such affiliate, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition.

"Unless there is in effect at the time an agreement filed with the Comptroller of the Currency pursuant to the terms of this section, any person, firm, corporation, association, business trust, or other organization, which shall vote, or cause, direct, authorize, or permit to be voted, the stock of any national bank owned or controlled by any affiliate, or by any officer, director, employee, proxy, nominee or representative or agent thereof, shall be deemed guilty of a misdemeanor and, upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 for each such offense. Each vote cast shall constitute a separate offense within the meaning of this paragraph."

It is recommended that, in lieu of section 20, there be inserted a new section 20 making similar requirements regarding holding companies which own or control State member banks of the Federal reserve system; and it is recommended that such new section 20 read as follows:

SEC. 20. The Federal reserve act, as amended, is further amended by inserting therein immediately after section 9 thereof a new section reading as follows:

"SEC. 9A. No State bank shall be permitted to become a member of the Federal reserve system unless any affiliate of such State bank or trust company, as defined in the banking act of 1932, which owns or controls such member bank directly or indirectly shall have filed with the Federal Reserve Board an agreement in such form as may be prescribed by such board accepting, and agreeing to submit to and comply with, all of the provisions of this section; and no State bank shall remain a member of the Federal reserve system after one year from the date of the enactment of this act unless any affiliate of such State bank which owns or controls such member bank directly or indirectly shall have filed such an agreement with the Federal Reserve Board.

"Within a period of one year from the date of any such agreement, each nonmember State bank owned or controlled by such affiliate which is eligible for membership in the Federal reserve system shall apply for membership therein in the manner prescribed by, and subject to the terms of, section 9 of this act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal reserve system and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any such bank shall fail to become, or cease to be, a member of the Federal reserve

system at any time while such agreement remains in effect, such affiliate shall divest itself of all of the stock ownership or other interest in, or control of, such bank.

"Except as provided herein, every such affiliate (1) on January 1, 1934, and at all times thereafter during the membership in the Federal reserve system of any state bank owned or controlled by it, shall possess, free and clear of any lien, pledge, or hypothecation of any nature, readily marketable assets other than bank stock, which shall not amount to less than 15 per centum of the aggregate par value of bank stocks held or owned by such affiliate; and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding, until its readily marketable assets, other than bank stocks, shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it: *Provided, however,* That, in computing the amount of readily marketable assets, other than bank stock, which any such affiliate is required to possess at any given time, credit shall be given to such affiliate for all contributions which it has made during the preceding three years to banks owned or controlled by it at the time such computation is made. The term 'contribution,' as herein used, shall include all such gifts of money, assets or other things of value to any such bank, all such amounts paid for worthless or doubtful assets purchased from any such bank, and all such other similar amounts as the Federal Reserve Board, in its discretion, may permit to be treated as contributions.

"If any such affiliate shall fail to comply with the provisions of this section or with the provisions of any agreement with the Federal Reserve Board made pursuant thereto, the said board, in its discretion, may require any state member bank owned or controlled by such affiliate to surrender its stock in the Federal reserve bank and to forfeit all rights and privileges of membership in the Federal reserve system as provided in section 9 of this Act.

"Any officer, director, agent, or employee of any such affiliate which has filed an agreement with the Federal Reserve Board, as provided in this section, who shall make any false entry in any book, report or statement of such affiliate with intent in any case to injure or defraud such affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such affiliate or of any member bank, or the Federal Reserve Board, or any agent or examiner appointed to examine the affairs of such affiliate, shall be deemed guilty of a misdemeanor, and upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No State member bank shall (1) make any loan on the stock of any affiliate which owns or controls such State member bank directly or indirectly, (2) make any loan to any affiliate which owns or controls such State member bank, directly or indirectly, on the security of any shares of stock of any corporation owned or controlled by such affiliate, or (3) be the purchaser or holder of the stock of such affiliate, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition."

Senator GLASS. From your own experience do you see any necessity for affiliates?

Mr. MEYER. Yes sir; there are a number of affiliates which you in the Congress authorized.

Senator GLASS. I mean those unauthorized by law.

Mr. MEYER. Yes.

Senator GLASS. We are not talking about these little inconsequential form matters.

Senator COUZENS. I should like to ask about affiliates built up outside of the law.

Mr. MEYER. Well, there are 15 different kinds of affiliates.

Senator COUZENS. I mean all those not authorized by law.

Mr. MEYER. There are realty companies, holding companies, bank building companies, mortgage companies, liquidating companies, agri-

cultural loan companies, personal or small loan companies, investment trusts, building and loan associations, insurance companies, finance and acceptance corporations, title and mortgage companies, and so on, I have a list here, as follows:

Number of nonbanking subsidiaries of national banks

Kind of affiliate	Mode of control				Total
	Stock owned by bank	Stock trusteeed	Stock owned by other affiliate	Stock owned by bank stock-holders	
Securities companies.....	4	126	17	45	192
Realty companies.....	4	33	8	110	155
Holding companies.....	4	28	7	31	70
Bank building companies.....	42	3	1	5	51
Safe deposit companies.....	33	4	3	4	44
Mortgage companies.....	2	11	6	18	37
Liquidating companies.....		6	3	28	35
Agricultural loan companies.....		6	3	26	35
Personal or small loan companies.....	1	10		16	27
Investment trusts.....	1	1	7	8	17
Building and loan associations.....		1	1	14	16
Insurance agencies.....		2	3	10	15
Finance and acceptance corporations.....		2	2	3	7
Title and mortgage guaranty companies.....		2	1	4	7
Foreign banks.....	3		3		6
Joint stock land banks.....		2	1	3	6
Title and mortgage companies.....	1		2		3
Investment houses, etc.....				1	1
Life or casualty insurance companies.....				1	1
Miscellaneous.....	3	8	13	21	45
Total.....	98	245	81	346	770

Senator GLASS. How many associations have ever been formed under the Edge Act?

Mr. MEYER. Not very many.

Senator GLASS. Only a few, and about all of those went out of business.

Mr. MEYER. Well, real estate holding companies for bank premises might be proper.

Senator COUZENS. The most objectionable one on the list is the investment affiliate.

Mr. MEYER. Yes, sir; and they are getting rid of those.

Senator COUZENS. Do you think we could eliminate those investment affiliates more promptly than to give them a 3-year period?

Mr. MEYER. I would rather hesitate to advise it, because I do not know what it would mean. I would hesitate to recommend too short a period. As a matter of fact if a period is set, or even if it is not, if information is being furnished in reports, I think the progress in the gradual and continuous elimination of undesirable affiliates would go right on. I see no disposition to acquire new affiliates for the handling of securities and, on the the other hand, I see a good deal of progress in the matter of elimination of them.

The CHAIRMAN. You would have no objection if we abolished it?

Senator GLASS. We have had testimony here that if we eliminate just those affiliates that are doing that wretchedly bad business, it will result in a great deal of deflation.

Mr. MEYER. Well, it is impossible to classify absolutely all affiliates that deal in securities as wicked and vicious.

Senator GLASS. We are not classifying all of them and we are not intending to reach all of them. There are some things that ought to be deflated. Stock gambling is one of them, and unloading on the portfolios of banks \$12,000,000 as foreign investment loans and things of that sort ought to be deflated; and any time is opportune to deflate them, in my judgment.

Mr. MEYER. I think we shall not disagree on that, Senator. But in reply to the Senator's direct question I am not prepared to say, because I do not know enough about that.

Senator COUZENS. As a matter of fact, practically all of these affiliates were developed by smart attorneys to evade the banking laws.

Mr. MEYER. Yes.

Senator COUZENS. Why should they be encouraged to be allowed to continue?

Mr. MEYER. I can not say, except that they were allowed to continue, and the Congress of the United States knew as well as anybody else that they were developed to evade the law.

Senator GLASS. Now, when we want to put a stop to them, we are told that the time is inopportune.

Mr. MEYER. A practice that has grown up with the semblance of legality, even though primarily designed to evade a law, because the authorities and the Congress of the United States did not object to it, although they knew all about it, gains a certain right to be treated with some consideration.

Senator COUZENS. It is one of those things that is allowed to go on when no trouble develops, and as soon as trouble develops, of course, everybody is wise.

Mr. MEYER. That is the way.

Senator COUZENS. The same thing happens, too, with your railroad holding companies.

Mr. MEYER. That is quite true. But, of course, these affiliates have been for the most part organized under State charters and differ fundamentally.

Senator GLASS. We can not interfere with that except when the affiliates of national banks do wrong we can step in and have something to say.

Mr. MEYER. The first of these security affiliates was, I believe, organized in 1908, Senator. Do you mean interference by the authorities or the Congress?

Senator GLASS. It has only in recent years come to the attention of Congress that they had been guilty of gross abuses and have created a great deal of distress in the country.

Mr. MEYER. Mind you, Senator, I quite agree, and the board does, with the general purpose and expresses sympathy with your attitude. In this particular case I think "when" may be important, although I do not know, because we have not the information. I am in hearty sympathy personally, I may say, Senator, with your desire to separate commercial banking from investment banking. That is what you really have in mind.

Senator GLASS. Some of the most experienced and reputable bankers in the United States came here and told us it ought to be done, that they were for abolishing them.

Senator COUZENS. Not only that; but the banks are carrying public advertisements now claiming they do not have affiliates in insurance companies.

Mr. MEYER. Some of them do.

Senator COUZENS. So it has got to be a discretionary practice; that when you have institutions merely merchandising securities, they are not to be called banks, are not to do a banking business.

Mr. MEYER. In section 21 there is nothing I wanted to comment on. I would leave it to the members of the committee to read.

Senator TOWNSEND. You recommend that section 19 be combined with section 20?

Mr. MEYER. Yes; in the way suggested in the memorandum.

Section 21. If the Committee on Banking and Currency decides to recommend the enactment of section 21 of the bill in substantially its present form, it is suggested that paragraph (d) of section 5155 of the Revised Statutes, (which forbids the establishment of any branch in a place with a population of less than 25,000) be amended in order that small communities may not be denied the banking facilities which otherwise might be provided under this section. It is also suggested that the second paragraph of section 9 of the Federal reserve act be amended so as to place State member banks on the same basis as national banks with respect to branches, either in this country or in foreign countries.

The sentence commencing in line 7 on page 46 of the bill might be substituted for paragraph (d) of section 5155 of the Revised Statutes; and the following might be added at the end of the second paragraph of section 9 of the Federal reserve act.

Then follows the suggestion for the amendment to be considered by the committee.

I will now turn to section 24 with the permission of the committee.

Senator GLASS. Does the board favor branch banking?

Mr. MEYER. The board did not take a vote on branch banking, because it is such a big subject and we did not have very much time for it. We had our experts analyzing the bill and explaining it to us for the best part of a week, and we just had two sessions of about three hours each and we did not get around to a thorough discussion of banking.

Senator GLASS. I have had this analysis of your experts on my table for a month.

Mr. MEYER. That was another analysis.

Senator GLASS. I have not observed any difference in it.

Mr. MEYER. On the subject of branch banking I should say the board would not be able to reach a unanimous expression Senator. There are some differences of opinion. Some forms of branch banking might be favored by some of us. We were not able in this document, which is unanimous on the points which are discussed, to express an opinion.

Senator GLASS. You want to put the entire responsibility of the solution of this unhappy problem on us, do you?

Mr. MEYER. You do not seem to worry about responsibility, and we feel you are amply equipped to handle it.

Senator GLASS. I have not done anything but worry for 14 months. [Laughter.]

Mr. MEYER. We feel the responsibility is on sturdy shoulders, Senator.

Senator GLASS. You do not seem to have much regard for the shoulders. [Laughter.]

Mr. MEYER. Of course, I will call your attention to this, Senator: As indicated in the letter transmitting the memorandum, it should be recognized that effective supervision of banking in this country has been seriously affected by the competition between member and nonmember banks. I think branch banking, under a unified banking system, would meet with a great deal of support. I know it would from me.

Senator GLASS. Can you suggest to us a constitutional method of creating a unified banking system in this country?

Mr. MEYER. Well, I do not know how to do that, but I believe it can be done by taxation or some other method. I do not think there is any doubt about the ability to do it. The principal thing about being able to do something is to want to do it.

Senator GLASS. We have wanted to do it.

Mr. MEYER. Do you want to bring about unified banking?

Senator GLASS. Why, undoubtedly; yes.

Mr. MEYER. I will be glad to help you.

Senator GLASS. I think the curse of the banking business of this country is the dual system.

Mr. MEYER. Then the board is entirely in sympathy with the committee on that subject.

Senator GLASS. Then let us get your recommendation.

Mr. MEYER. We will try to prepare one for you.

Senator GLASS. Let us get it quickly, then, if you please.

Mr. MEYER. We saw no evidence in the bill that there was such a desire.

Senator GLASS. I do not suppose that I violate any confidence when I said that the board went to the extent of trying to obtain and did obtain an opinion from the Attorney General of the United States, and he could not suggest to us any method of doing it.

Mr. MEYER. I do not know whether the opinion was in reply to questions which covered all the possible ways of doing it. I certainly think it can be done, although I am not a lawyer. I do know, however, that competition between the State and National banking systems has resulted in weakening both steadily.

Senator GLASS. I say so, yes; and I have not been afraid when we come to tackle a question of that sort. There are more State banks than there are national banks, and very likely more State bankers would vote against me than national bankers would vote for me. But that does not bother me the least in the world. If you will simply suggest a constitutional way of doing the thing I will try to put it through.

Senator WALCOTT. Governor, while we are on that: I do not think it is betraying any confidence to say the members of the subcommittee would go even as far as the districts of the Federal reserve system in making 35 branch districts, but we never could get it through Congress. The subcommittee, I think, would unanimously go as far as States with an exception on border-line towns within a

radius of 50 or a hundred miles such as the bill provides for. There have been witnesses here that have been familiar with and have been very active in the group banking business that have testified unless they could have some provision for branch banking at least state-wide, irrespective of State lines, that it would be the doom of the group system; they must have an escape from the group banking.

The CHAIRMAN. The Senator will recall that some of the witnesses of the group system a year ago had the opposite view.

Senator WALCOTT. Yes.

The CHAIRMAN. And appeared before this same committee on this same bill.

Senator WALCOTT. Exactly.

The CHAIRMAN. In other words, they told us that 40 years of experience led to a judgment against branch banks. Now they say they have had 41 and they have changed their minds. [Laughter.]

Senator WALCOTT. And they emphasized by saying that they must have the branches.

The CHAIRMAN. In other words, they want to abandon experience for a theory. They want to try a theory.

Mr. MEYER. The next is section 24. I shall not detain you much longer. You have been very patient.

Senator FLETCHER. Before you turn away from section 21. In the testimony this morning before this committee Mr. Wakefield particularly recommended line 21 on page 45, that you strike out the words "if such establishment and operation are at the time permitted to State banks by the law of the State in question."

Mr. MEYER. If you strike that out, of course, the chances are that immediately every one of those States would pass a law that would authorize State branch banking, would they not?

Senator WALCOTT. It might be a sound law, though.

Senator FLETCHER. I see that it might. I think it would have that effect and might be a good thing.

Mr. MEYER. I am not prepared to give an offhand opinion on that.

Senator FLETCHER. He suggests that as an amendment to this bill. I should like to get something out of what we have before us. I would like an opinion as to whether that would cure the situation or would be beneficial or helpful.

Mr. MEYER. If you get a sound banking foundation, you can discuss the details of superstructure. I am more interested in the possibility of the committee going into a plan for unified banking, because it would simplify many of those questions which you are now discussing.

Senator GLASS. You have your experts.

Mr. MEYER. I will see if we can do anything for you. May I then go on with the views of the board?

Section 24: While it is recognized that certain evils arise from the competitive bidding for deposits through the payment of unduly high rates, it is believed that it is undesirable to further regulate by law the rates of interest, which may be paid on deposits, especially since to do so would place member banks at a disadvantage in competition with nonmember banks. It is, therefore, recommended that this section be omitted.

That is just an illustration of the inability to put sound regulations in force on account of the competition that has to be met all the time.

Section 26: It is recommended that this section be omitted entirely.

It would apply to all loans on "collateral security" regardless of the nature of the security, and would nullify certain provisions of section 5200 of the Revised Statutes, including those permitting national banks to make loans (1) in amounts not exceeding 25 per cent of their capital and surplus on the security of shipping documents or chattel mortgages on live stock, and (2) in amounts not exceeding 50 per cent of their capital and surplus on the security of shipping documents.

Senator FLETCHER. We have had a great deal of difficulty about that word "collateral."

Mr. MEYER. We feel that the words "collateral security" would include a great deal that you do not intend.

Senator GLASS. What do you suppose they meant by it when they used it over and over again in these proposed amendments?

Mr. MEYER. They do not mean exclusively "collateral" loans. It is used in the vernacular to mean what you use it to mean in this bill; but its legal meaning is not confined to that, in the opinion of our experts.

Senator FLETCHER. What does "collateral" mean?

Mr. MEYER. It means in addition to and on the side. [Laughter.] In other words, you could get your money on an unsecured note but somebody else would have to put up collateral security in addition to his note.

Senator GLASS. What do you experts mean by the use of the words here—and this is one of a dozen instances? [Reading:]

No national banking association and no member bank shall (1) make any loan or any extension of credit to any affiliate organized and existing for the purpose of buying and selling stocks, bonds, real estate, or real-estate mortgages, or for the purpose of holding title to any such property, or (2) invest any of its funds in the capital stock, bonds, or other obligations of any such affiliate, or (3) accept the capital stock, bonds, or other obligations of any such affiliate as collateral security to protect loans made to any person.

And so forth and so on. And further down:

Investments and advances against such collateral security which will exceed 10 per centum.

Mr. MEYER. It mentions specifically there what the collateral security is.

Senator GLASS. No.

Mr. MEYER. Oh, yes.

Senator GLASS (reading):

Agreements, investments, and advances against collateral security which will exceed 10 per centum of the capital stock.

And so forth. Those are just two of a dozen instances in which the term "collateral security" is used.

Mr. MEYER. In talking to-day on this very point with a gentleman from Chicago, he said that in Chicago collateral security was more usually warehouse receipts for grain than anything else. It is a question of what the words mean.

Senator GLASS. I know. The question is what sense we have used them in. We use them to indicate stocks, and bonds.

Mr. MEYER. Senator, you know since I saw a decision of the Supreme Court that Congress meant one thing while the chairman and members of the committee told me that they meant another thing, I have not been able to feel that the intent of the committee

was conclusive when it came to the courts; and I think the language ought to be clear if you do not want to do harm.

Senator GLASS. If it is in one provision and in another provision, I do not see the difference.

Mr. MEYER. I think it would cover many things besides stocks and bonds as collateral security.

Senator GLASS. You know very well what we intended to cover. Mr. MEYER. Surely.

Section 29: Section 29 provides for the removal of officers or directors of national banks under certain circumstances. It is believed that there should be some means by which in extreme cases unsatisfactory management could be corrected through the removal of officers and directors responsible therefor.

It is believed, however, that the power of removal should be vested in the Federal Reserve Board as a whole rather than in a special committee consisting of three officials, one of whom is the person bringing the charges against the accused officer or director; and, in order to afford adequate additional protection to the interests of the banks and their officers and directors, certain other changes in this section should be made. It is, therefore, recommended that section 29 be amended to read as follows:

And suggestions are made as to the changes which the board thinks are advisable and necessary for their protection.

Senator GLASS. Getting back to the proposition, Governor, that you said you were going to have a provision—I have not observed that you have come to it at all—about the deflationary nature of the provision of this bill with respect to real-estate loans. You said that the limitation was too severe, and I observe here that you make it more severe. [Reading:]

Any such bank may make such loans in an aggregate sum including in such aggregate any such loans on which it is liable as indorser or guarantor or otherwise equal to 15 per centum of the amount of capital stock of such association actually paid in and unimpaired and 15 per centum of its unimpaired surplus fund.

That is just exactly what you testified. And then you go on to say: "Or to one-third of its savings deposits."

That was one-half. It seems to me that your proposition is more deflationary than ours.

Mr. MEYER. I think the phraseology there was concerned with the appraisals which we felt—

Senator GLASS. Oh, no.

Mr. MEYER. Senator, are you reading from the Burgess-Goldenweiser report?

Senator GLASS. Yes. I am reading from the bill that these gentlemen sent up here—your experts.

Mr. MEYER. Well, Senator, this is a new report that I am making for the board.

Senator GLASS. I have not observed much change.

Mr. MEYER. I think there are quite a lot of changes and some additions, and I do not think we have followed that report in all details. I am sure that we did not in the matter that you are reading.

Senator WALCOTT. What section is that?

Senator GLASS. We will come to that.

Mr. MEYER. I am not recommending that, Senator.

Senator GLASS. We will come to that.

Mr. MEYER. We did not recommend the section which you quote.

Senator GLASS. That is one case in which you changed your mind.

Mr. MEYER. The Burgess-Goldenweiser report is not a report of the board and was only seen by the board after it had been delivered to the subcommittee.

Senator GLASS. The board and Doctors Burgess and Goldenweiser seem to have had one mind.

Mr. MEYER. Not entirely. That is proven by your quotation.

Senator GLASS. There are some inconsequential differences, I note.

The CHAIRMAN. Have you finished?

Mr. MEYER. Yes, Mr. Chairman. I thank you for your patience.

The CHAIRMAN. I asked you that in order that the members of the committee may be informed. I am sure some of them have refrained from asking questions since you made that request.

Mr. MEYER. I am very much obliged to you for that courtesy.

The CHAIRMAN. They will have their chance to ask you questions now.

Senator GLASS. I do not want to ask him any.

The CHAIRMAN. Any further questions?

Mr. MEYER. I would like to ask, Mr. Chairman, if the memorandum which I have presented on behalf of the board, along with the letter, may be introduced into the record in complete form. I read most of the important sections.

The CHAIRMAN. Without objection that will be, but do you not want it in connection with your testimony and your side remarks?

Mr. MEYER. I would; yes.

Senator WALCOTT. Do you want your comments printed separately?

The CHAIRMAN. They will be out of line unless they go together as your testimony.

Mr. MEYER. Yes; but I would like the letter and the complete memorandum without the conversation and my comment introduced.

The CHAIRMAN. Also printed in a separate place?

Mr. MEYER. Complete, and as an exhibit to the hearings, if it is agreeable.

The CHAIRMAN. Any objections?

Senator BROOKHART. Do you think this bill ought to pass?

Mr. MEYER. I think the board feels that the bill with the suggested amendments would be good legislation and ought to pass.

Senator BROOKHART. And if the amendments are not adopted, then what?

Mr. MEYER. We have not canvassed the board on that point.

Senator GLASS. You deal with many important problems, quite as many as the subcommittee has dealt with. Do you think that now is an inopportune time to make any of these alterations in the banking structure?

Mr. MEYER. I think that when the board sends a memorandum suggesting changes in a piece of legislation and expressing general sympathy with the purpose of the bill, it has taken a position in support of the measure in a general way, subject, of course, to its views as to particular clauses.

Senator GLASS. The board suggests certain amendments to the proposed bill. What I am asking you is whether you think or whether

the board thinks this is an opportune time to consider those amendments dealing with extremely vital and important bank matters or to legislate at all?

Mr. MEYER. I think any legislation, Senator, to be considered at this time ought to be most carefully considered from the viewpoint of its time relation to the present economic and financial conditions. I think it is a difficult time to legislate and the greatest care should be used that any bill which is passed should not be restrictive of credit and that it should not be disturbing to confidence. I am frank to say that I think the reserve provisions in the bill as written would be disturbing on account of the increase in the reserves provided for in the bill. I think it is not a question whether a bill is a good thing to pass at this time. I do not think that is a fair question.

Senator GLASS. Of course, any bill affecting the banking business of the country ought to be seriously considered, and I am sure you do not mean to imply that this subcommittee has not seriously considered all of these problems over a long period of time and has not endeavored to the fullest extent to get the intelligent and uninfluenced judgment of men who are competent to speak.

Mr. MEYER. No; I am quite sure that the committee has worked very industriously over a long period, but I still would not like to say that a bill would be a good thing to pass because I do not think it is a proper question. The question is whether a particular bill would be a good bill to pass at any particular time.

Senator GLASS. That is exactly what I am asking. If we should adopt the amendments proposed by the Federal Reserve Board, do you think the bill thus amended, dealing with these vital problems of banking, should be now passed?

Mr. MEYER. I think it could be passed without danger and with a good deal of benefit.

Senator GLASS. I am not even saying that it could be passed at all. I am asking you whether you think it should be passed at this time.

Mr. MEYER. Yes; I think it should. As amended, I would welcome its passage. There has, of course, to be borne in mind the fact that the question as to separation of affiliates, in our minds, is in the realm of the unknown to a certain extent, because of the absence of full information, and the board offers no strong recommendation although it submits a suggestion. But on the other measures I think the board would welcome the passage of the bill with the amendments.

The CHAIRMAN. I begin to think this Federal Reserve Board and this banking committee are not so far apart.

Mr. MEYER. Who said we were, Senator?

Senator GLASS. I do. [Laughter.]

Mr. MEYER. I was wondering. You think we are so far apart, Senator?

Senator GLASS. You express some considerable sympathy with our point of view of things.

Mr. MEYER. Yes. I think we are not far apart. I think there is, in principle, no great divergence.

Senator GLASS. Speaking of the affiliate problem, I had a real good nice rest last night for the first time in a long time after reading over twice and scrutinizing very carefully the affiliate provision drafted by your experts. It is so akin to the one that we had in here,

with, possibly, the exception of definitions, that I felt very much encouraged to think that we had such good authority on the subject.

Mr. MEYER. Well, Senator, I am glad you slept well. I can not say that as to myself after I got notice late yesterday afternoon that I had to appear here.

Senator GLASS. I have not observed you had that language in your statement.

Mr. MEYER. It is a long section there.

Senator GLASS. You just did not read it?

Mr. MEYER. Yes.

Senator GLASS. It is a pretty good one, I think.

Mr. MEYER. I do not know that ours is identical.

Senator GLASS. I do not say "identical." I said "akin."

Mr. MEYER. It is a rather hard thing to define. It is one of the most difficult definitions.

Senator GLASS. It is a hard thing to define, and we have been trying to get somebody to define it for us; that is, the meaning of "collateral security." One of the distinguished and long-experienced bankers who has testified at these hearings after a little bantering agreed to attempt to give us his definition, and we will give it due consideration.

Mr. MEYER. The subject that you have been working out in your committee—better banking—is, I think, the most important public question before the country, and the board sincerely desires to cooperate with this committee in every way, and has always been desirous of doing so, and we are glad to be able to offer you an expression of the board which, so far as it goes, is the joint and unanimous expression of all of the members of the board.

Senator BROOKHART. In 1928 and 1929 that great deflation was the cause of our present reaction and depression, was it not?

Mr. MEYER. The great inflation all over the world was perhaps the principal cause of the present collapse and depression all over the world.

Senator BROOKHART. Investment bankers and others had sold these inflated bonds of foreign countries and also domestic bonds to our people everywhere, had they not?

Mr. MEYER. No doubt. Of course.

Senator BROOKHART. Did the policy of the Federal Reserve Board have anything to do with that?

Mr. MEYER. I was not a member of the board at that time, Senator.

Senator BROOKHART. You know what the board did?

Mr. MEYER. I do not know what they did. Senator, I can not testify on what the board did in 1928 or did not do. I know that I expressed my opinion of a great many of these securities to such officials as I met when I had an opportunity, and I even sought the opportunity. I did that, however, in my personal and private capacity, and I had no official relation to the problem.

Senator BROOKHART. You noticed there was a problem, did you not, at that time?

Mr. MEYER. I think a great many people did, Senator.

Senator BROOKHART. Did not you pay any attention to the policy of the Federal Reserve Board in reference to that problem?

Mr. MEYER. That is four years ago, Senator. I would not like to testify about what I did in 1928 on matters with which I had no official connection.

Senator BROOKHART. How many bank failures have there been in the United States since you have been governor of the board?

Mr. MEYER. A great many.

Senator BROOKHART. More than usual?

Mr. MEYER. Yes.

Senator BROOKHART. Was that because you were governor? [Laughter.] Or was it because—

Mr. MEYER. Well, I will say that in the month of March the number of banks closed was equalled by the number of banks opened, substantially, and that the resources of the banks opened were larger than the resources of banks closed; and that is the best record that has been made in four years in the United States which include two and one half years when I was not governor.

Senator BROOKHART. That is what happened in one month there?

Mr. MEYER. Well, that is the present condition.

Senator BROOKHART. What I was interested in was whether or not the policy of the board had anything to do with the bringing on of the inflation.

Mr. MEYER. You mean in 1928 and 1929?

Senator BROOKHART. Yes.

Mr. MEYER. I can not testify back of September, 1930. There has been no inflation since then. I am sorry to say there has been too much deflation, but when these forces once get under way they are hard to stop.

Senator BROOKHART. You think this bill would stop that kind of performance in the future?

Mr. MEYER. I think it would help to do so and make for better banking, especially if you can find a way to bring about unified banking in the country.

Senator GLASS. You are going to do that for us.

Mr. MEYER. The first thing is to find out whether you want to do it.

Senator GLASS. I told you that we do.

Mr. MEYER. I heard it to-day for the first time.

Senator BROOKHART. I am willing to do it on a cooperative principle. [Laughter.]

APPENDIX

MARCH 29, 1932.

HON. PETER NORBECK,

Chairman, Committee on Banking and Currency,

United States Senate, Washington, D. C.

DEAR SENATOR NORBECK: On March 17, 1932. I received a letter from Senator Glass inclosing copies of Senate bill 4115, and stating that the Banking and Currency Committee would be glad to have the Federal Reserve Board make any comments or suggestions that in its judgment would seem desirable. Accordingly, there is inclosed herewith for the consideration of your committee a memorandum containing the board's comments and recommendations.

The subjects dealt with in the bill may be classified under three general heads: (1) Those relating more directly to the Federal Reserve Board and the reserve banks, (2) those concerning primarily member banks, and (3) those dealing with affiliates of member banks.

The Federal Reserve Board is in sympathy with the purpose of the bill to strengthen the supervision of the Federal reserve system over general credit

conditions and to invest the Federal reserve authorities with certain disciplinary powers in relation to banks that pursue unsafe and unsound policies or abuse the privileges of membership. The board's recommendations on this subject are incorporated in its proposed revision of sections 3 and 29 of the bill.

With respect to the section of the bill dealing with open market operations, the board calls attention to the fact that there is already in existence an open market committee on which each of the Federal reserve banks has representation. This has come about as the result of natural development. The board believes that it would be inadvisable to disturb this development by crystallizing into law any particular procedure. The board believes that nothing further is necessary or advisable at this time than an amendment clarifying its power of supervision over open market operations of the Federal reserve banks and their relationships with foreign banks, as set out in the memorandum attached.

The board is not in sympathy with the provisions of the bill discriminating against member bank collateral notes. Experience shows that the particular instrument on which Federal reserve credit is obtained is not an adequate test of the use to be made by the member bank of the proceeds of the credit and that an attempt to control speculation through restrictions on member bank collateral notes would not be effective in accomplishing the purpose of this section of the bill. Indeed, it probably would interfere seriously with the convenient and economical operation of the system. In this connection, the Federal Reserve Board desires to renew the recommendation made in its annual reports for several years, that the maturity for which advances may be made to member banks on their promissory notes secured by paper which is eligible for discount be increased from 15 to 90 days. Such an amendment would be especially helpful to country banks.

The board is of the opinion that the adoption of a system of reserves based on velocity of accounts as well as on their volume, as recommended by the system's committee on reserves, would be an important step in strengthening the influence that the Federal reserve system could exert in the direction of sound credit conditions. The section of the bill dealing with reserves would accentuate rather than reduce the inequalities that have grown up in the distribution of reserves between different classes of member banks. The board also believes it should not be overlooked that this section of the bill would exert a tightening influence on credit conditions at times when it would be contrary to the public interest.

The board is in favor of establishing a liquidating corporation, but proposes to limit the scope of its operations to member banks and suggests a different method of financing it, together with certain changes in the provisions for its administration.

If the section on branch banking is enacted in the form proposed in the bill, it is suggested that certain sections of existing law be modified so as to bring them into harmony with the purposes indicated in this section of the bill.

With respect to affiliates, the board believes that important reforms to be accomplished at the present time are the granting of power to the supervisory authorities to obtain reports and to make examinations of all affiliates of member banks and the prescribing of limitations on the loans that a member bank may make to its affiliates. The board realizes that many evils have developed through the operation of affiliates connected with member banks, particularly affiliates dealing in securities. The attached memorandum contains a draft of a provision for the separation of such affiliates after a lapse of three years.

The board takes the view that legislation further materially restricting the character of member bank loans and investments is not desirable at a time when the country's banking system is going through a period of severe readjustment. Some of the provisions of the proposed bill would have a tendency to bring about further contraction of credit and thus retard the recovery of business. It is for these reasons that changes in a number of sections of the bill are suggested.

It should be recognized that effective supervision of banking in this country has been seriously hampered by the competition between member and non-member banks, and that the establishment of a unified system of banking under national supervision is essential to fundamental banking reform.

Copies of this letter and the inclosed memorandum are being sent to Senator Glass, and the board will be glad to supply you with copies for the convenience of each member of your committee.

Very truly yours,

EUGENE MEYER, *Governor.*

COMMENTS AND RECOMMENDATIONS REGARDING SENATE BILL 4115

[All references are to sections, pages, and lines of S. 4115 in the form in which it was introduced on March 14 (calendar day, March 17), 1932]

Section 2: This section defines affiliates and upon its scope depends in a large measure the scope and effect of all provisions of the bill relating to affiliates.

While the definition contained in the bill mentions certain specific types of institutions which are frequently affiliated with member banks, the words "or a corporation" in line 4, on page 2, make it applicable to corporations of any character which are affiliated with member banks in any of the ways described in the succeeding paragraphs of the definition.

It is believed that the most satisfactory solution of this problem is to make the definition very broad but, in dealing with affiliates, to observe the following principles: (1) To require them to make reports and to submit to examination at the discretion of the board or the comptroller; (2) to limit the loans that can be extended to an affiliate by a member bank; and (3) to prohibit the tying up of capital stock of an affiliate with the capital stock of a member bank. In favoring these limitations, the board has in mind that it may not be desirable to abolish all the existing relationships between member banks and their affiliates, but that it is desirable to protect the operations of the member banks from being unduly influenced by their affiliates. Recent experience has demonstrated that operations of the affiliates at times have unfavorable effects on the condition of member banks.

With these principles in mind, it is recommended that the definition of affiliates be broadened by eliminating from paragraph (b) in lines 1 to 4, page 2, all references to specific types of corporations, and by inserting other words which would make the definition applicable not only to corporations but to business trusts, associations, or other similar organizations, regardless of the type of business in which they are engaged. Certain other changes in the phraseology of the definition are also suggested for the purpose of clarifying them. The changes suggested are as follows:

1. On page 2, change lines 1 to 4, inclusive, to read as follows:

"(b) The term 'affiliate' includes any corporation, business trust, association or other similar organization."

2. In lines 9, 11, and 22, on page 2, strike out the words "managing officers" and substitute in lieu thereof the words "persons exercising similar functions."

3. In lines 9 and 18 on page 2, and in line 3 on page 3, strike out the words "annual meeting" and substitute in lieu thereof the word "election."

Section 3: The Federal Reserve Board understands that the principles underlying section 3 of the bill are (1) that discounting at the Federal reserve banks is a privilege and not a right; (2) that the Federal reserve system has the responsibility of keeping itself informed about the use of bank credit; (3) that the power of Federal reserve banks to withhold credit accommodations should be used to discourage unsound banking practices; and (4) that the Federal Reserve Board should have power to suspend a member bank from the use of Federal reserve credit facilities. The board is in sympathy with these principles.

For the purpose of accomplishing these objectives, a substitute for section 3 is suggested. This substitute includes a revision of the paragraph of section 4 of the Federal reserve act which now reads as follows:

"Said board shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and shall, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements, and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks."

In this revision the word "may" is substituted for "shall" and the remaining language of the section is made somewhat more general than in the bill.

Member banks as a rule do not borrow to relend, but to make up deficiencies in reserves arising from withdrawals of deposits or from other causes. It is, therefore, usually impossible to say that a loan to a member bank is granted for this or that specific purpose. However, it would be possible to determine whether the loan and investment policies of a bank are inconsistent with the purposes of the Federal reserve act, and, if so, to refuse accommodation to such bank or in aggravated cases to suspend it from the privilege of using the system's credit facilities. In this connection attention is invited to the fact that section 4 of the Federal reserve act requires the chairman and Federal reserve agent at each Federal reserve bank to "make regular reports to the

Federal Reserve Board" and to "act as its official representative for the performance of the functions conferred upon it by" the Federal reserve act.

It is recommended that section 3 of the bill be changed to read as follows:

"SEC. 3. The paragraph of section 4 of the Federal reserve act, as amended, which begins with the words, 'Said board shall administer the affairs of said bank fairly and impartially,' is amended and reenacted to read as follows:

"Said board of directors shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and may, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks, the maintenance of sound credit conditions and the accommodation of commerce, industry, and agriculture. The Federal Reserve Board may prescribe regulations further defining within the limitations of this act the conditions under which discounts, advancements and accommodations may be extended to member banks. Each Federal reserve bank shall keep itself informed of the general character and amount of the loans and investments of its member banks with a view to ascertaining whether undue use is being made of bank credit for the speculative carrying of or trading in securities, real estate or commodities, or for any other purpose inconsistent with the maintenance of sound credit conditions; and, in determining whether to grant or refuse advances, rediscunts or other credit accommodations, the Federal reserve bank shall give consideration to such information. The chairman of the Federal reserve bank shall report to the Federal Reserve Board any such undue use of bank credit by any member bank, together with his recommendation. Whenever, in the judgment of the Federal Reserve Board, any member bank is making such undue use of bank credit, the board may, in its discretion, after reasonable notice and an opportunity for a hearing, suspend such bank from the use of the credit facilities of the Federal reserve system and may terminate such suspension or may renew it from time to time."

Section 4: It is recommended that this section be omitted. It prohibits banks that belong to a group or a chain from voting for Federal reserve bank directors. The wording of the section is such as not to confine the prohibition to group and chain banks, however, but to include all banks that are not controlled entirely by locally resident stockholders. Since the stock of many important banks is widely owned throughout the country, this might restrict the voting privilege to smaller and less important banks that are owned by local stockholders. It is to be feared that this section would bar from participation in the selection of Federal reserve directors many of the better-managed banks.

Section 5: This section would amend the first paragraph of section 7 of the Federal reserve act so that, after the payment of expenses and dividends, all of the net earnings of a Federal reserve bank over and above any amounts necessary to restore its surplus to the amount on December 31, 1931, would be paid to the Federal liquidating corporation. The amendment is also worded in such a way as to prevent the payment of any dividends out of surplus and to prevent the payment of dividends whenever the surplus of a Federal reserve bank is less than it was on December 31, 1931.

A different method of financing the liquidating corporation is proposed and will be discussed under the appropriate section. For this reason a modification of section 5 is suggested which would not change the provisions of the present law in regard to the surplus of the Federal reserve banks, but would authorize the Secretary of the Treasury to use the franchise tax received from the Federal reserve banks for the purpose of supplementing the funds of the corporation.

As changed, section 5 of the bill would read as follows:

"SEC. 5. The second paragraph of section 7 of the Federal Reserve act, as amended, is amended to read as follows:

"The net earnings derived by the United States from Federal reserve banks shall, in the discretion of the Secretary of the Treasury, (1) be used to supplement the gold reserve held against outstanding United States notes, or (2) be applied to the reduction of the outstanding bonded indebtedness of the United States under regulations to be prescribed by the Secretary of the Treasury, or (3) be invested in debentures or other such obligations of the Federal liquidating corporation. Should a Federal reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts,

dividend requirements as hereinbefore provided, and the par value of the stock, shall be paid to and become the property of the United States and shall be similarly applied."

Section 6: In order that reports of affiliates of State member banks may be required only when deemed necessary by the Federal Reserve Board and also in order that suitable provision may be made for the examination of affiliates of State member banks when deemed necessary, it is recommended that section 6 of the bill be changed to read as follows:

"Sec. 6. Section 9 of the Federal reserve act, as amended, is further amended by adding at the end thereof two new paragraphs reading as follows:

"Whenever it shall be deemed necessary in order to obtain adequate information regarding the relations between any bank admitted to membership under the provisions of this section and its affiliates or the effect of such relations upon the management or condition of such bank, it may be required under rules and regulations prescribed by the Federal Reserve Board to obtain and furnish such reports as to any or all of its affiliates as may be called for. Each such report shall contain such information and shall be submitted at such time as may be specified in the call therefor. Any member bank which fails to furnish any report of an affiliate when and as required shall be subject to a penalty of \$100 for each day during which such failure continues. Such penalty may be assessed by the Federal Reserve Board, in its discretion, and, when assessed, may be collected by the Federal reserve bank by suit or otherwise.

"Any examiner selected or approved by the Federal Reserve Board may examine any affiliate of any bank admitted to membership under the provisions of this section when it shall be deemed necessary in order to inform the Federal Reserve Board or the Federal reserve bank of the relations of such affiliate with such member bank or of the effect of such relations upon the management or condition of such member bank. The examiner making the examination of any such affiliate shall have power to make a thorough examination of all the affairs of the affiliate, and in doing so he shall have power to administer oaths and to examine any of the officers, directors, employees, and agents thereof under oath, and to make a report of his findings to the Federal Reserve Board or to the Federal reserve bank. The expenses of any examination made under the provisions of this paragraph may, in the discretion of the Federal Reserve Board, be assessed against the affiliate examined and, when so assessed, shall be paid by the affiliate examined. If such affiliate shall refuse to pay such expenses or shall fail to do so within sixty days after the date of such assessment, then such expenses may be assessed against the affiliated member bank and, when so assessed, shall be paid by such member bank; *Provided, however*, That if the affiliation is with two or more member banks, such expenses may be assessed against, and collected from, any or all of such member banks in such proportions as the Federal Reserve Board may prescribe. If any affiliate of a bank admitted to membership under the provisions of this section shall refuse to permit an examiner to make an examination of such affiliate or refuse to give any information required in the course of any such examination, the member bank with which it is affiliated shall be subject to a penalty of not more than \$100 for each day that any such refusal shall continue. Such penalty may be assessed by the Federal Reserve Board in its discretion, and, when so assessed, may be collected by the Federal reserve bank by suit or otherwise."

Section 7: If this section is adopted in its present form, certain changes should be made in the text for the purpose of clarification and of providing for certain matters not now covered in the bill which will be referred to at the appropriate places.

For the purposes of clarification, it is suggested that subsection (b) be amended as follows:

1. In lines 6, 11, and 12, on page 8, it is suggested that the word "appointive" be inserted before the word "member."

2. In line 13, on page 8, it is suggested that after the words "12 years" there be inserted the words "from the expiration of the term of his predecessor."

In order that the domicile of the board may be fixed for legal reasons, and in order that provision may be made for a chairman of the board, it is suggested that the following be inserted at the beginning of line 23 on page 8:

The principal offices of the board shall be in the District of Columbia. At meetings of the board, the governor shall preside as chairman, and, in his absence, the vice governor shall preside. In the absence of both the governor

and the vice governor, the board shall elect a member to act as chairman *pro tempore*.

If the authority of the Secretary of the Treasury to assign quarters to the Federal Reserve Board is repealed, it would seem that the board should be authorized to purchase or construct a building for its own use and that, in the interest of convenience and efficiency, space should be provided in such building for the Comptroller of the Currency and his staff and for the proposed Federal liquidating corporation. For this purpose, it is suggested that the following be added at the end of section 7 of the bill:

"(d) Section 10 of the Federal reserve act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

"The Federal Reserve Board is authorized and empowered to acquire by purchase, condemnation, or otherwise, a building located in the District of Columbia which will provide suitable and adequate offices wherein the functions of the board and the Comptroller of the Currency may be carried on, or to acquire by purchase, condemnation, or otherwise, such site located in the District of Columbia as it may deem necessary and to cause to be constructed thereon a building which will provide suitable and adequate offices for the purposes of the Federal Reserve Board and the Comptroller of the Currency, and to maintain, repair, enlarge, or remodel any building so acquired or constructed. The Federal Reserve Board may assign offices in any such building for the use of the Comptroller of the Currency and the Federal liquidating corporation without making any charge for the use of such offices, and nothing contained in the act of June 3, 1864, or in section 331 of the Revised Statutes (title 12, sec. 13, U. S. C.), or in any other provision of law, shall be construed as preventing the Comptroller of the Currency from making full use of any offices so assigned and from keeping therein the records and all other valuable things belonging to his department. The Federal Reserve Board may levy upon the Federal reserve banks, in proportion to their capital stock and surplus, assessments sufficient to defray all costs and expenses incurred under the provisions of this paragraph."

Section 8. The purpose of this section is to prevent the undue use of bank loans for speculation in securities. It is believed that this is sufficiently covered in section 3, and, therefore, the omission of section 8 is recommended.

Section 9: In accordance with the principles indicated in the discussion of section 2, it is recommended that section 9 of the bill be changed to read as follows:

"Sec. 9. The Federal reserve act, as amended, is amended by inserting between sections 23 and 24 thereof the following new section:

"Sec. 23 (a). No national banking association and no State member bank shall (1) make any loan or any extension of credit to, or purchase securities under repurchase agreement from, any of its affiliates; or (2) invest any of its funds in the capital stock, bonds, or other obligation of any such affiliate; or (3) accept the capital stock, bonds, or other obligations of any such affiliate as collateral security for advances made to any individual, partnership, association, or corporation; if, in the case of any such affiliate, the aggregate amount of such loans or extensions of credit, repurchase agreements, investments, and advances against such collateral security will exceed 10 per centum of the capital stock and surplus of such national banking association or State member bank, or if, in the case of all such affiliates, the aggregate amount of such loans, extensions of credit, investments, and advances against such collateral security will exceed 20 per centum of the capital stock and surplus of such national banking association or State member bank: *Provided, however*, That nothing in this section, or in any section of the banking act of 1932, shall be construed as authorizing member banks to invest their funds in stock otherwise than as specifically authorized by existing law.

"Each loan or extension of credit to an affiliate within the foregoing limitations shall be secured by collateral having a market value at the time of making the loan or extension of credit of at least 20 per centum more than the amount of such loan: *Provided*, That this requirement shall not apply to loans or extensions of credit on the security of obligations of the United States Government; Reconstruction Finance Corporation, Federal intermediate credit banks, or Federal land banks, or on the security of notes, drafts, bills of exchange, or acceptances eligible for discount or purchase by Federal reserve banks: *And provided further*, That when any loan is made on the security of obligations of any State or political subdivision or agency thereof such obligations shall have a market value at the time of making the loan of at least 10 per centum more than the amount of such loan. A loan or extension of credit to a director,

officer, clerk, or other employee or any representative of any such affiliate shall be deemed a loan to the affiliate to the extent that the proceeds of such loan are used for the benefit of, or transferred to, the affiliate.

"The provisions of this section shall not apply to any affiliate of such national banking association or State member bank (1) the sole function of which is to hold its banking house or houses and the site or sites thereof, (2) the sole function of which is to conduct a safe deposit business, (3) in the capital stock of which such bank has been authorized to invest pursuant to section 25 of the Federal reserve act, (4) organized under section 25 (a) of the Federal reserve act, or (5) transacting only the business of an agricultural credit corporation or livestock loan company; but as to such affiliates member banks shall continue subject to the provisions of existing law limiting the amounts which they may lend to, or invest in the stock or other obligations of, such corporations."

Section 10: This section of the bill deals with two separate and distinct subjects—(1) open market operations of the Federal reserve banks, and (2) The proposed Federal liquidating corporation. For convenience, these subjects will be discussed separately.

OPEN-MARKET OPERATIONS

The first part of section 10 would establish a Federal open-market committee along the lines of the existing open-market policy conference which functions as a piece of administrative machinery without specific legal status.

The statement in paragraph (b) of section 10 which says that "No Federal reserve bank shall engage in open-market operations, except after approval and authorization by the committee," appears to be too rigid. It deprives an individual reserve bank of all authority to make purchases in the open market except after obtaining the consent of both the board and the committee. The open-market committee would have no authority to act without approval of the board and the board would have no authority to act without approval of the committee. This would result in the possibility of obstruction of any system program and would tend to make the operation of the Federal reserve system less timely and less efficient.

Lines 19 to 23 in paragraph (c) on page 12 of this section would incorporate into law a principle which the Federal Reserve Board has adopted in practice.

The following substitute for the first part of section 10 of the bill is suggested:

"Sec. 10. Section 14 of the Federal reserve act, as amended, is further amended by striking out the words 'Every Federal reserve bank shall have power'; and inserting in lieu thereof the following:

"Subject to such regulations, limitations, restrictions, and procedure as the Federal Reserve Board may prescribe, every Federal reserve bank shall have power."

"Section 14 of the Federal reserve act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

"The time, character, and volume of all purchases and sales in the open market under this section shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country."

FEDERAL LIQUIDATING CORPORATION

The other part of section 10 deals with the proposed Federal liquidating corporation, and there is submitted a proposed substitute for the section as drafted in the bill. The substitute would confine the benefits of the liquidating corporation to member banks. Provision is made for assistance to nonmember banks in the Reconstruction Finance Corporation act, and it would render membership in the system more attractive if the benefits of the corporation were confined to member banks. In the substitute it is proposed that \$100,000,000 of the capital of the liquidating corporation be subscribed by the Treasury. This subscription to capital may be considered as being derived from the franchise tax previously paid to the Treasury by the reserve banks. In addition, it is proposed that the corporation be authorized to issue debentures up to twice the amount of its subscribed capital and that the Federal reserve banks be given authority to purchase those debentures up to one-fourth of their surplus. This is not a propitious time to ask the member banks to contribute to the liquidating corporation. The banks are going through a very

difficult period and to tax them for this purpose would be a considerable hardship on them.

In order to make the operations of the corporation more easily manageable, it is proposed that the directorate be comprised of five members instead of fourteen as proposed in the bill.

For the reasons which have been stated the following separate section on the Federal liquidating corporation has been drafted:

"Sec. 5 A. The Federal reserve act, as amended, is further amended by inserting between sections 28 and 29 thereof the following new section:

"SEC. 28 A. (a) There is hereby created a Federal liquidating corporation (hereafter referred to as the "corporation") for the purpose of making loans on, or purchasing and liquidating as hereinafter provided, all or any part of the assets of any member bank for which a receiver has been appointed. The term "receiver" as used in this section shall mean a receiver of a national bank, and a receiver, liquidating agent, commission, person, or other agency charged by State law with the responsibility and the duty of winding up the affairs of an insolvent State member bank.

"(b) The management of the corporation shall be vested in a board of directors consisting of five members, one of whom shall be the Comptroller of the Currency, one a member of the Federal Reserve Board designated by the board for the purpose, and three selected annually by the governors of the twelve Federal reserve banks under such procedure as may be prescribed by the Federal Reserve Board.

"(c) The corporation shall have a capital stock of \$100,000,000, all of which shall be subscribed by the United States of America and payment for which shall be subject to call in whole or in part by the board of directors of the corporation.

"There is hereby authorized to be appropriated out of any money in the Treasury not otherwise appropriated the sum of \$100,000,000 for the purpose of making payments upon such subscription. Receipts for payments by the United States for or on account of such stock shall be issued by the corporation to the Secretary of the Treasury and shall be evidence of the stock ownership of the United States.

"Any Federal reserve bank may purchase and hold any debentures or other such obligations of the corporation in an amount not exceeding one-fourth of the amount of its surplus fund.

"(d) The corporation shall have power—

"First. To adopt, alter, and use a corporate seal.

"Second. To have perpetual succession from the date of enactment hereof, unless it is sooner dissolved by an act of Congress.

"Third. To make contracts; to purchase, lease, and hold or dispose of such real estate or personal property as may be necessary or convenient for the transaction of its business.

"Fourth. To sue and be sued, complain and defend in any court of competent jurisdiction.

"Fifth. To appoint, employ, and fix the compensation of such officers, employees, attorneys, and agents as shall be necessary for the transaction of the business of the corporation, without regard to the provisions of other laws applicable to the employment and compensation of officers or employees of the United States, to define their authority and duties, to require bonds of them and fix the penalty thereof and to dismiss them at pleasure. Nothing in this or any other act shall be construed to prevent the appointment and compensation as a director, officer, or employee of the corporation of any officer or employee of the United States in any board, commission, independent establishment, or executive department thereof.

"Sixth. To prescribe, amend, and repeal by its board of directors by-laws and rules and regulations not inconsistent with law governing the manner in which its general business may be conducted and the privileges granted to it by law may be exercised and enjoyed.

"Seventh. To exercise such incidental powers as shall be reasonably necessary to carry out the powers so granted.

"(e) The board of directors of the corporation shall determine and prescribe the manner in which its obligations shall be incurred and its expenses allowed and paid. The corporation shall be entitled to the free use of the United States mails in the same manner as the executive departments of the Government. The corporation with the consent of any Federal reserve bank or of any board, commission, independent establishment, or executive department of the Government, including any field service thereof, may avail itself of the use

of information, services, and facilities thereof in carrying out the provisions of this act.

“(f) Upon the application of the receiver of any member bank, the corporation may in its discretion purchase the assets of such bank, in whole or in part, or make loans to the receiver on the security of such assets or any portion thereof, on such terms and conditions as shall be agreed upon between the corporation and the receiver, subject to the approval of (1) the Comptroller of the Currency in the case of any national bank, or (2) the person or agency designated by State law in the case of any State bank; except that, in no case shall the corporation make any loan or purchase any assets in an amount which in the opinion of the corporation shall not fully protect such corporation and no such loan or purchase shall be made in the case of State member banks unless expressly authorized by the law of the State in which the bank is located. Receivers of national banks are hereby authorized and empowered with the approval of the Comptroller of the Currency to borrow on, or sell, assets of banks of which they are receivers, and the proceeds of every such sale or loan shall be utilized for the same purposes and in the same manner as other funds realized from the liquidation of the assets of such banks. The Comptroller of the Currency may, in his discretion, pay dividends on proved claims at any time after the expiration of the period of advertisement made pursuant to section 5235 of the Revised Statutes, and no liability shall attach to the Comptroller of the Currency or to the receiver of any national bank by reason of any such payment for failure to pay dividends to a claimant whose claim is not proved at the time of any such payment. If the amount realized from any assets acquired by the corporation under the provisions of this section exceeds the sum paid therefor or loaned thereon, the corporation shall make an additional payment to the receiver of the bank equal to the amount of such excess, if any, after deducting the expenses of liquidating such assets and an amount equal to interest at the rate of 6 per centum per annum. All loans made by the corporation to receivers shall bear interest at the rate of 6 per centum per annum.

“(g) Money of the corporation not otherwise employed shall be invested in securities of the Government of the United States, except that for temporary periods, in the discretion of the board of directors, funds of the corporation may be deposited subject to check in any Federal reserve bank or with the Treasurer of the United States. When designated for that purpose by the Secretary of the Treasury, the corporation shall be a depository of public moneys, except receipts from customs, under such regulations as may be prescribed by the said Secretary, and may also be employed as a financial agent of the Government. It shall perform all such reasonable duties as depository of public moneys and financial agent of the Government as may be required of it.

“(h) The corporation is authorized and empowered to issue and to have outstanding at any one time in an amount aggregating not more than twice the amount of its capital, notes, debentures, bonds, or other such obligations, to be redeemable at the option of the corporation before maturity in such manner as may be stipulated in such obligations, to bear such rate or rates of interest, and to mature at such time or times as may be determined by the corporation: *Provided*, That the corporation may sell on a discount basis short-term obligations payable at maturity without interest. Obligations of the corporation may be secured by assets of the corporation in such manner as shall be prescribed by the board of directors. Such obligations may be offered for sale at such price or prices as the corporation may determine. The said obligations shall be fully and unconditionally guaranteed both as to interest and principal by the United States and such guaranty shall be expressed on the face thereof. In the event that the corporation shall be unable to pay upon demand, when due, the principal or of interest on notes, debentures, bonds, or other such obligations issued by it, the Secretary of the Treasury shall pay the amount thereof, which is hereby authorized to be appropriated, out of any moneys in the Treasury not otherwise appropriated, and thereupon to the extent of the amounts so paid the Secretary of the Treasury shall succeed to all the rights of the holders of such notes, debentures, bonds, or other such obligations.

“(i) All obligations issued by the corporation shall be exempt, both as to principal and interest, from all taxation (except estate or inheritance taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing

authority. The corporation, including its franchise, its capital, reserves, and surplus, and its income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority, except that any real property of the corporation shall be subject to State, county, municipal, or local taxation to the same extent according to its value as other real property is taxed.

"(j) In order that the corporation may be supplied with such forms of obligations as it may need for issuance under this act, the Secretary of the Treasury is authorized to prepare such forms as shall be suitable and approved by the corporation, to be held in the Treasury subject to delivery, upon order of the corporation. The engraved plates, dies, bed pieces, and other material executed in connection therewith shall remain in the custody of the Secretary of the Treasury. The corporation shall reimburse the Secretary of the Treasury for any expenses incurred in the preparation, custody, and delivery of such obligations.

"(k) The corporation shall annually make a report of its operations to the Congress as soon as practicable after the 1st day of January in each year.

"(l) Whoever, for the purpose of obtaining any loan from the corporation, or any extension or renewal thereof, or the acceptance, release, or substitution of security therefore, or for the purpose of inducing the corporation to purchase any assets, or for the purpose of influencing in any way the action of the corporation under this act, makes any statement, knowing it to be false, or willfully overvalues any security, shall be punished by a fine of not more than \$5,000, or by imprisonment for not more than two years, or both.

"(m) Whoever (1) falsely makes, forges, or counterfeits any obligation or coupon, in imitation of or purporting to be an obligation or coupon, issued by the corporation, or (2) passes, utters, or publishes, or attempts to pass, utter, or publish, any false, forged, or counterfeited obligation or coupon, purporting to have been issued by the corporation, knowing the same to be false, forged or counterfeited, or (3) falsely alters any obligation, or coupon, issued or purporting to have been issued by the corporation, or (4) passes, utters, or publishes, or attempts to pass, utter, or publish as true, any falsely altered or spurious obligation or coupon, issued or purporting to have been issued by the corporation, knowing the same to be falsely altered or spurious, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

"(n) Whoever, being connected in any capacity with the corporation, (1) embezzles, abstracts, purloins, or willfully misapplies any moneys, funds, securities, or other things of value, whether belonging to it or pledged, or otherwise entrusted to it, or (2) with intent to defraud the corporation or any other body, politic or corporate, or any individual, or to deceive any officer, auditor, or examiner of the corporation, makes any false entry in any book, report, or statement of or to the corporation, or without being duly authorized draws any order or issues, puts forth, or assigns any note, debenture, bond, or other such obligation, or draft, bill of exchange, mortgage, judgment, or decree thereof, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

"(o) No individual, association, partnership, or corporation shall use the words "Federal Liquidating Corporation", or a combination of these three words, as the name or a part thereof under which he or it shall do business. Every individual, partnership, association, or corporation violating this subdivision shall be punished by a fine of not exceeding \$1000, or by imprisonment not exceeding one year, or both.

"(p) The provisions of sections 112, 113, 114, 115, 116, and 117 of the Criminal Code of the United States (U.S.C., title 18, ch. 5, secs. 202 to 207, inclusive), in so far as applicable, are extended to apply to contracts or agreements with the corporation under this act, which for the purposes hereof shall be held to include loans, advances, extensions and renewals thereof, and acceptances, releases, and substitutions of security therefor, purchases or sales of assets, and all contracts and agreements pertaining to the same.

"(q) The Secret Service Division of the Treasury Department is authorized to detect, arrest, and deliver into the custody of the United States marshal having jurisdiction any person committing any of the offenses punishable under this section."

Section 11: Section 11 imposes a discriminatory rate against member bank collateral notes. It also prescribes limitations on the use of such notes by banks that may be making loans on stock exchange collateral. It is believed

that the purposes of this section are accomplished by the proposed revision of section 8 and that no further limitations along this line are desirable. The theory underlying this section, namely, that there is a more direct connection between member bank collateral notes and the use of reserve credit for speculative activity than between other borrowings and this activity is unfounded. Member banks borrow on 15-day notes, because of the greater convenience both to them and to the Federal reserve bank; and, if this form of borrowing were prohibited or made more expensive, they would merely substitute the procedure of rediscounting eligible paper without any change in the use of the proceeds. For these reasons, it is believed that this section would make the operation of the Federal reserve banks less efficient and more expensive.

The recommendation has been made by the Federal Reserve Board in its annual reports for several years that the maturity for which advances may be made to member banks on their promissory notes secured by paper which is eligible for discount be increased from 15 to 90 days. Such an amendment would be especially helpful to country banks, and it is recommended that the following be substituted for section 11 of the bill:

"Sec. 11. The seventh paragraph of section 13 of the Federal reserve act, as amended, is amended and reenacted to read as follows:

"Any Federal reserve bank may make advances for periods not exceeding fifteen days to its member banks on their promissory notes secured by the deposit or pledge of bonds, notes, certificates of indebtedness or treasury bills of the United States; and any Federal reserve bank may make advances for periods not exceeding ninety days to its member banks on their promissory notes secured by such notes, drafts, bills of exchange or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this act. All such advances shall be made at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board."

Section 12. Section 12 deals with relations of Federal reserve banks with foreign banks. It is recommended that the words "subject to the powers conveyed to and bestowed upon the Federal open market committee by section 12 A of this act" be omitted. From the middle of line 18 on page 26 through the word "writing" in line 11 on page 27, the section is acceptable, but the omission of the words "and control" in line 19 on page 26 is suggested, in order to preserve the distinction between supervision and operation.

It is recommended, therefore, that section 12 of the bill be amended as follows:

- (1) Strike out the following language in lines 16, 17, and 18 on page 26: "(g) Subject to the powers conveyed to and bestowed upon the Federal open market committee by section 12 A of this act";
- (2) Strike out the words "and control" in line 19 on page 26; and
- (3) On page 27, line 11, insert a period after the word "writing" and strike out everything in line 11 after that word and all of lines 12, 13, 14, and 15.

Section 13: The principal feature of this section is that it discontinues the distinction between time deposits and demand deposits in so far as reserve requirements are concerned. The distinction between these two types of deposits has led to many abuses and has been a factor in making possible a growth of bank credit without a corresponding growth in reserves. The proposal which would raise the requirements on time deposits to the level of those on demand deposits would increase reserve requirements by \$132,000,000 a year for five years with an ultimate increase of \$660,000,000. Unless there were a contraction in the amount of member bank deposits, this increase would result in an addition of about \$230,000,000 to the gold requirements of the Federal reserve banks. It would be an influence in the direction of credit contraction without regard to the course of business and credit and would be particularly undesirable at this time. Furthermore, the increase would fall heaviest on banks outside of the principal financial centers, which have been discriminated against under the existing reserve requirements both because, owing to their distance from the cash facilities of the Federal reserve banks, they are required to carry relatively large amounts of cash in vault, which under existing law does not count as reserve, and because they are not in a position to take advantage of deductions in determining net deposits.

The proposal, therefore, would both increase the burden of reserves and increase the inequalities in their present distribution.

Any thorough-going revision of section 19 of the Federal reserve act should base required reserves, in so far as practicable, upon the activity of the business handled through each bank, rather than on an arbitrary classification of

banks according to location. A proposal submitted in the Report of the Committee on Bank Reserves of the Federal Reserve System embodies a method of calculating required reserves which is believed to be sound in principle and which would make fluctuations in the volume of required reserves exert an influence in the direction of sound credit conditions and would also eliminate many inequitable and unfair features of the present law.

There is submitted a proposed substitute for section 13 of the bill which incorporates the proposals of the committee on bank reserves of the Federal reserve system with slight modifications.

Section 13 includes two subjects not directly related to bank reserves and not covered in the report of the reserve committee, namely, a prohibition against brokers' loans for the account of others and a provision subjecting the market for Federal funds to regulation by the Federal Reserve Board.

The purpose sought to be accomplished by paragraph (d) is desirable, but it is believed that the language used is too far reaching. It is suggested that the paragraph be changed so as to prohibit a member bank from acting as a medium or agent of a nonbanking corporation or individual in making loans on the security of stocks, bonds, and other investment securities to brokers or dealers in such securities. This suggestion is incorporated in paragraph (n) of the proposed revision of section 13 of the bill. It is not thought that a provision prohibiting a member bank from making loans to any corporation or individual if the proceeds of such transaction are to be used directly or indirectly for the purpose of making loans protected by collateral security in favor of any investment banker, broker, or member of any stock exchange or any dealer in securities, would be enforceable as it is impossible to follow the proceeds of loans once they have been granted.

Paragraphs (f) and (g) of the bill seek to control the market for Federal funds by placing limitations on the use of balances standing to the credit of member banks upon the books of the Federal reserve banks. It is not believed that regulation of the market for Federal funds by law is desirable. It is better to have these liquid funds move freely where they are most needed than to have them thrown on the call market. The Federal reserve banks keep in close touch with transactions in Federal funds and a ruling of the Federal Reserve Board now requires member banks to report purchases of Federal funds as borrowed money.

The proposed substitute for section 13 of the bill is as follows:

"Sec. 13. Section 19 of the Federal reserve act (U. S. C., title 12, secs. 461 to 466, inclusive, and sec. 374), as amended, is further amended and reenacted to read as follows:

"RESERVES OF MEMBER BANKS

"Sec. 19. (a) Each member bank shall establish and maintain reserves equal to 5 per centum of the amount of its net deposits, plus 50 per centum of the amount of its average daily debits to deposit accounts: *Provided*, That any member bank, at its option, for any period not less than ninety days, may, omit any specific deposit account or accounts from such computation of its reserve requirements if such account or accounts are reported separately to the Federal reserve bank and if a reserve of 50 per centum is maintained against such account or accounts: *Provided, however*, That, in no event, shall the aggregate reserves required to be maintained by any member bank exceed fifteen per centum of its gross deposits.

"(b) Each member bank located in the vicinity of a Federal reserve bank or branch thereof shall maintain not less than four-fifths of its total required reserves in the form of a reserve balance on deposit with the Federal reserve bank, and every other member bank shall maintain not less than two-fifths of its total required reserves in the form of a reserve balance on deposit with the Federal reserve bank. The remainder of the total required reserves of each member bank, over and above the amount required to be maintained in the form of a reserve balance on deposit with the Federal reserve bank, may, at the option of such member bank, consist of a reserve balance on deposit with the Federal reserve bank, or of cash owned by such member bank either in its actual possession or in transit between such member bank and the Federal reserve bank: *Provided*, That when, in its judgment the public interest so requires, the Federal Reserve Board may limit to an amount less than that permitted hereunder the amount of cash which any member bank or banks may count as reserve: *Provided, however*, That, in prescribing such limitations, the Federal Reserve Board shall be guided by the general principle that member banks should be permitted to count as reserve, within the limitations of

this section, as much cash as they reasonably need in view of the character of their business and their degree of accessibility to the currency facilities of the Federal reserve banks.

"(c) The term "gross deposits," within the meaning of this section, shall include all deposit liabilities of any member bank whether or not immediately available for withdrawal by the depositor, all liabilities for certified checks; cashiers', treasurers', and other officers' checks; cash letters of credit; travelers' checks; and all other similar liabilities, as further defined and specified by the Federal Reserve Board: *Provided, however,* That, in computing the amount of "gross deposits," (1) amounts shown on the books of any member bank as liabilities of such bank payable to a branch of such bank located in a foreign country or in a dependency or possession of the United States, and (2) liabilities payable only at such a branch, shall be treated as though said liabilities were due to or payable at a nonmember bank.

"(d) The term "net deposits," as used in this section, shall mean the amount of the gross deposits of any member bank, as above defined and as further defined by the Federal Reserve Board, minus the sum of (1) all balances due to such member bank from other member banks and their branches in the United States, and (2) checks and other cash items in process of collection which are payable immediately upon presentation in the United States, within the meaning of these terms as further defined by the Federal Reserve Board.

"(e) The term "average daily debits to deposit accounts," as used in this section, shall mean the average daily amount of checks, drafts, and other items debited or charged by any member bank to any and all accounts included in gross deposits as above defined and as further defined by the Federal Reserve Board, except charges resulting from the payment of certified checks and cashiers', treasurers', and other officers' checks.

"(f) The term "cash," within the meaning of this section, shall include all kinds of currency and coin issued or coined under the authority of the laws of the United States.

"(g) The term "reserve balances," as used in this section, shall mean a member bank's actual net balance on the books of the Federal reserve bank representing funds available for reserve purposes under regulations prescribed by the Federal Reserve Board.

"(h) The term "vicinity of a Federal reserve bank or branch thereof," as used in this section, shall mean the city in which a Federal reserve bank or branch thereof is located, until such term is otherwise defined by the Federal Reserve Board: *Provided,* That, with respect to each Federal reserve bank and each branch thereof, the Federal Reserve Board, from time to time, in its discretion, may either (1) define a specific geographic area as comprising the vicinity of such Federal reserve bank or branch thereof, within the meaning of this section, or (2) compile a list of member banks which shall be deemed to be located in the vicinity of such Federal reserve bank or branch thereof, within the meaning of this section, and add banks to, or remove banks from, such list, from time to time: *Provided, however,* That, in defining such areas and compiling such lists, the Federal Reserve Board shall be guided, by the general principle indicated in subsection (b) hereof.

"(i) With respect to each member bank, the term "Federal reserve bank," as used in this section, shall mean the Federal reserve bank of the district in which such member bank is located.

"(j) The Federal Reserve Board is authorized and empowered to prescribe regulations defining further the various terms used in this act, fixing periods over which reserve requirements and actual reserves may be averaged, determining the methods by which reserve requirements and actual reserves shall be computed, and prescribing penalties for deficiencies in reserves. Such regulations and all other regulations of the Federal Reserve Board shall have the force and effect of law and the courts shall take judicial notice of them.

"(k) Subject to such regulations and penalties as may be prescribed by the Federal Reserve Board, any member bank may draw against or otherwise utilize its reserves for the purpose of meeting existing liabilities: *Provided, however,* That, whenever the reserves of any member bank have been continuously deficient for fourteen consecutive calendar days, the Federal reserve agent or assistant Federal reserve agent of the district in which such member bank is located shall send to each director of such bank, by registered mail, a letter advising him of such deficiency and calling attention to the provisions of this subsection; and each director of such bank who after receipt of such a letter, assents to or acquiesces in the making of additional loans or investments

by such bank before the reserves of such bank shall have been restored to the amount required by this section, shall be held liable in his personal or individual capacity for any and all losses sustained by such bank on any such loans or investments.

"(l) All penalties for deficiencies in reserves incurred under regulations prescribed by the Federal Reserve Board pursuant to the provisions of this act shall be paid to the Federal reserve bank by the member bank against which they are assessed.

"(m) No member bank shall keep on deposit with any State bank or trust company which is not a member bank a sum in excess of ten per centum of its own paid-up capital and surplus. No member bank shall act as the medium or agent of a nonmember bank in applying for or receiving discounts from a Federal reserve bank under the provisions of this act, except by permission of the Federal Reserve Board.

"(n) No member bank shall act as the medium or agent of any nonbanking corporation, partnership, association, business trust, or individual in making loans on the security of stocks, bonds, and other investment securities to brokers or dealers in stocks, bonds, and other investment securities. Every violation of this provision by any member bank shall be punishable by a fine of not more than \$100 per day during the continuance of such violation; and such fine may be collected, by suit or otherwise, by the Federal reserve bank of the district in which such member bank is located.

"(o) National banks or banks organized under local laws, located in Alaska, or in a dependency or insular possession or any part of the United States outside the continental United States, may remain nonmember banks, and shall in that event maintain reserves and comply with all the conditions now provided by law regulating them; or said banks may, with the consent of the Federal Reserve Board, become member banks of any one of the Federal reserve districts, and shall in that event take stock, maintain reserves, and be subject to all the other provisions of this act.

"(p) All acts or parts of acts in conflict with this section are hereby repealed only in so far as they are in conflict with the provisions of this section."

"There are hereby repealed the provisions of section 7 of the first liberty bond act, approved April 24, 1917, section 8 of the second liberty bond act, approved September 24, 1917, and section 8 of the third liberty bond act, approved April 4, 1918 (U. S. C., title 31, sec. 771) which read as follows:

"That the provisions of section 5191 of the Revised Statutes, as amended by the Federal reserve act, and the amendments thereof, with reference to the reserves required to be kept by national banking associations and other member banks of the Federal reserve system, shall not apply to deposits of public moneys by the United States in designated depositories."

"This section shall become effective on the first day of the seventh calendar month following the enactment of this act."

Section 14: The first portion of this section down to line 4 on page 33 is existing law. The sentence in lines 4 to 8, inclusive, is new and would interfere greatly with the financing of real estate transactions. When a time loan has been made there appears to be no warrant, in the absence of default, for revising the valuations on which the loan is based; and this provision, together with that in lines 4 to 9 on page 34, would require the real estate on which each such loan is based to be revalued at least five times each year. It could not reasonably be expected that real estate loans would be made or applied for under such conditions.

The sentence in lines 17 to 20 on page 33 would classify as real estate loans all unsecured loans whose eventual safety depends upon the value of real estate, thereby subjecting all such loans to all the limitations or restrictions in this section. This would produce confusion and uncertainty in a large volume of loans and would interfere with the extension of adequate credit, particularly in the agricultural sections of the country.

The remaining amendments in this section make what appear to be unnecessary changes in the proportion of the real estate loans permitted and proposed, without segregation, to give time depositors a preferred claim on all real estate loans and other assets of the bank acquired under this section. Such a provision would be difficult to administer and would be unfair to the other depositors.

The sentence in lines 15 to 22 on page 34 is existing law and is inconsistent with section 24 of the bill, which will be discussed later.

It would seem desirable to limit the amount which banks may invest in bank premises, but it is suggested that this be accomplished directly instead of indirectly.

It is recommended, therefore, that section 14 of the bill be stricken out and that the following new section be substituted:

"Sec. 14. The Federal reserve act, as amended, is amended by inserting between section 24 and section 25 thereof the following new section:

"Sec. 24 (a). Except with the permission of the Comptroller of the Currency, no national bank, and except with the permission of the Federal Reserve Board, no State member bank, shall hereafter invest in bank premises or in the stock or obligations of, or in loans to, any corporation owning or holding its bank premises a sum exceeding the amount of the capital stock of such bank."

Section 15: This section would make it necessary for member banks to dispose of a large amount of securities at this time which would be very unfortunate. Since it is aimed generally at investments in securities, it is believed that its purpose is covered sufficiently by the proposed substitute for section 3 of the bill.

The clause commencing in line 19 on page 35 apparently is intended to enable national banks to compete more effectively with State banks. Its tendency would be to lower the standards of banking in the national banking system to the standard of the State banks, where more liberal powers are granted to State banks by State law.

The definition of investment securities which is contained in the law, as amended by the act of February 25, 1917, would be stricken out and apparently the comptroller would be given unlimited power to prescribe his own definition except that stocks could not be included. This modification is undesirable.

For the reasons stated, it is recommended that this section be omitted entirely.

Section 16: This amendment is believed to be desirable; but it is recommended that it be strengthened and that a means of evasion be eliminated by striking out the exception in lines 17 to 21, inclusive, on page 37, which would permit the organization of national banks with a capital of \$25,000 in certain circumstances.

Section 17: The modification of the units in which bank stocks can be issued would create unnecessary complications; and it is recommended that all of section 17 be omitted, with the exception of the sentence in lines 17 to 23 on page 38, which should be made effective not less than three years after enactment.

As modified, section 17 would read as follows:

"Sec. 17. Section 5139 of the Revised Statutes, as amended, is amended by adding at the end thereof a new paragraph reading as follows:

"After three years from the date of the enactment of this act, no certificate representing the stock of any such association shall represent the stock of any other corporation, nor shall the ownership, sale or transfer of any certificate representing the stock of any such association be conditioned in any manner whatsoever upon the ownership, sale, or transfer of a certificate representing the stock of any other corporation."

Section 18: The first part of this section would prohibit any director, officer, or employee of any member bank from acting as a director, officer, or employee of certain other specified classes of business enterprises. It would be capable of easy evasion and would become ineffective in many cases. The latter part of the section would prohibit any member bank from clearing checks or doing the ordinary banking business of a correspondent for any of the types of business enterprises mentioned in this section. The language of the section is so broad that it would include banks within the classes of business enterprises to which the prohibitions of the section would apply. For example, all interlocking bank directorates now expressly authorized by law or permitted under certain conditions would be prohibited, and one bank would be prohibited from acting as a correspondent of another bank. It is, therefore, recommended that this entire section be omitted.

It has been clearly demonstrated that affiliations between member banks and security companies have contributed to undesirable banking developments. There are, however, difficulties in the way of accomplishing a complete divorce of member banks from their affiliates arising from the fact that a law intended for that purpose is likely to be susceptible of evasion or else to apply to many cases to which it is not intended to apply. Therefore, the board is

not prepared at this time to make a definite recommendation, but submits, for the consideration of the Committee on Banking and Currency, a substitute for section 18 which is designed to provide for the divorce of security affiliates from member banks after three years:

"Sec. 18. From and after three years from the date of the enactment of this act, no member bank shall be affiliated in any manner described in section 2 (b) hereof with any corporation, association, business trust, or other similar organization engaged principally in the issue, flotation, underwriting, public sale, or distribution at wholesale or retail, of stocks, bonds, debentures, notes, or other securities.

"For every violation of this section, the member bank involved shall be subject to a penalty not exceeding \$1,000 per day for each day during which such violation continues. Such penalty may be assessed by the Federal Reserve Board, in its discretion, and, when so assessed, may be collected by the Federal reserve bank by suit or otherwise.

"If any such violation shall continue for six calendar months after the member bank shall have been warned by the Federal Reserve Board to discontinue the same, (a) in the case of a national bank, all the rights, privileges, and franchises granted to it under the national bank act may be forfeited in the manner prescribed in section 5239 of the Revised Statutes, or, (b) in the case of a State member bank, all of its rights and privileges of membership in the Federal reserve system may be forfeited in the manner prescribed in section 9 of the Federal reserve act."

Sections 19 and 20: It is recommended that section 19 of the bill be combined with section 20 in the manner hereinafter proposed; that the combined section be known as section 19; and that a new section applicable to holding companies which own or control State member banks be substituted for section 20.

Under the definition of "affiliate" contained in section 2 and under the provisions of sections 6, 27, and 28 of the bill, if amended in accordance with the recommendations contained in this report, all holding companies which control member banks and all banks owned or controlled by such holding companies will be affiliates of such member banks and will be required to make reports and submit to examinations whenever deemed necessary or advisable by the Comptroller of the Currency, the Federal Reserve Board or examiners appointed by them; and, therefore, it is suggested that the provisions regarding examinations and condition reports of holding companies be omitted from this section and from the corresponding sections regarding holding companies which own or control State member banks.

It is also suggested that there be inserted in section 19 and in the proposed new section 20 certain additional provisions providing for the regulation and supervision of holding companies and requiring all eligible State banks controlled by them to be members of the Federal reserve system.

It is, therefore, recommended that section 19 of the bill be changed to read as follows:

"Sec. 19. Section 5144 of the Revised Statutes, as amended, is amended to read as follows:

"Sec. 5144. In all elections of directors and in deciding all questions at meetings of shareholders, each shareholder shall be entitled to one vote on each share of stock held by him, except that shares of its own stock held by any national bank as trustee shall not be voted, and shares owned or controlled by any affiliate, as defined by the banking act of 1932, or by any officer, director, employee, proxy, nominee, or representative, or agent thereof, shall not be voted unless such affiliate shall have filed with the Comptroller of the Currency an agreement in such form as may be prescribed by him accepting, and agreeing to submit to and comply with, all of the provisions of this section, and such agreement shall not have been terminated. Shareholders may vote by proxies duly authorized in writing; but no officer, clerk, teller, or bookkeeper of such association shall act as proxy; and no shareholder whose liability is past due and unpaid shall be allowed to vote.

"Within a period of one year from the date of any such agreement, each nonmember State bank owned or controlled by such affiliate which is eligible for membership in the Federal reserve system shall apply for membership therein in the manner prescribed by, and subject to the terms of, section 9 of the Federal reserve act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal reserve system and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any

such bank shall fail to become, or shall cease to be, a member of the Federal reserve system at any time while such agreement remains in effect, such affiliate shall divest itself of all stock ownership or other interest in, or control of, such bank.

"Except as otherwise provided herein, every such affiliate, (1) on January 1, 1934, and at all times thereafter while such agreement remains in effect, shall possess, free and clear of any lien, pledge, or hypothecation of any nature, readily marketable assets other than bank stock, which shall not amount to less than 15 per centum of the aggregate par value of bank stocks held or owned by such affiliate, and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding, until its readily marketable assets other than bank stocks shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it; *Provided, however, That, in computing the amount of readily marketable assets, other than bank stock, which any such affiliate is required to possess at any given time, credit shall be given to such affiliate for all contributions which it has made during the preceding three years to banks owned or controlled by it at the time such computation is made. The term "contribution," as herein used, shall include all such gifts of money, assets or other things of value to any such bank, all such amounts paid for worthless or doubtful assets purchased from any such bank, and all such other similar amounts as the Comptroller of the Currency, in his discretion, may permit to be treated as contributions.*

"If any such affiliate shall fail to comply with the provisions of this section or with the provisions of any agreement with the Comptroller of the Currency made pursuant thereto, the Comptroller, in his discretion, may terminate such agreement.

"Any officer, director, agent, or employee of any such affiliate, which has entered into an agreement with the Comptroller of the Currency in accordance with the provisions of this section, who shall make any false entry in any book, report or statement of such affiliate with intent in any case to injure or defraud such affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such affiliate or of any member bank, or the Comptroller of the Currency, or any agent or examiner appointed to examine the affairs of such affiliate, shall be deemed guilty of a misdemeanor and upon conviction thereof in any district court of the United States shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No National bank shall (1) make any loan on the stock of any affiliate which owns or controls such National bank directly or indirectly, (2) make any loan to any affiliate which owns or controls such National bank, directly or indirectly, on the security of any shares of stock of any corporation owned or controlled by such affiliate, or (3) be the purchaser or holder of the stock of such affiliate, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition.

"Unless there is in effect at the time an agreement filed with the Comptroller of the Currency pursuant to the terms of this section, any person, firm, corporation, association, business trust, or other organization, which shall vote, or cause, direct, authorize, or permit to be voted, the stock of any national bank owned or controlled by any affiliate, or by any officer, director, employee, proxy, nominee or representative or agent thereof, shall be deemed guilty of a misdemeanor and, upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 for each such offense. Each vote cast shall constitute a separate offense within the meaning of this paragraph."

It is recommended that, in lieu of section 20, there be inserted a new section 20 making similar requirements regarding holding companies which own or control State member banks of the Federal reserve system; and it is recommended that such new section 20 read as follows:

"Sec. 20. The Federal reserve act, as amended, is further amended by inserting therein immediately after section 9 thereof a new section reading as follows:

"Sec. 9A. No State bank shall be permitted to become a member of the Federal reserve system unless any affiliate of such State bank or trust company, as defined in the banking act of 1932, which owns or controls such member bank, directly or indirectly, shall have filed with the Federal Reserve Board an agree-

ment in such form as may be prescribed by such board accepting, and agreeing to submit to and comply with, all of the provisions of this section; and no State bank shall remain a member of the Federal reserve system after one year from the date of the enactment of this act unless any affiliate of such State bank which owns or controls such member bank, directly or indirectly, shall have filed such an agreement with the Federal Reserve Board.

"Within a period of one year from the date of any such agreement, each nonmember State bank owned or controlled by such affiliate which is eligible for membership in the Federal reserve system shall apply for membership therein in the manner prescribed by, and subject to the terms of, section 9 of this act. If such application is approved by the Federal Reserve Board, such bank shall become a member of the Federal reserve system and shall comply with all of the provisions of law applicable to member banks. If such application is not approved by the Federal Reserve Board, or if any such bank shall fail to become, or cease to be, a member of the Federal reserve system at any time while such agreement remains in effect, such affiliate shall divest itself of all of the stock ownership or other interest in, or control of, such bank.

"Except as provided herein, every such affiliate (1) on January 1, 1934, and at all times thereafter during the membership in the Federal reserve system of any State bank owned or controlled by it, shall possess, free and clear of any lien, pledge or hypothecation of any nature, readily marketable assets other than bank stock, which shall not amount to less than 15 per centum of the aggregate par value of bank stocks held or owned by such affiliate, and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding, until its readily marketable assets, other than bank stocks, shall amount to 25 per centum of the aggregate par value of bank shares held or owned by it: *Provided, however,* That, in computing the amount of readily marketable assets, other than bank stock, which any such affiliate is required to possess at any given time, credit shall be given to such affiliate for all contributions which it has made during the preceding three years to banks owned or controlled by it at the time such computation is made. The term "contribution," as herein used, shall include all such gifts of money, assets or other things of value to any such bank, all such amounts paid for worthless or doubtful assets purchased from any such bank, and all such other similar amounts as the Federal Reserve Board, in its discretion, may permit to be treated as contributions.

"If any such affiliate shall fail to comply with the provisions of this section or with the provisions of any agreement with the Federal Reserve Board made pursuant thereto, the said board, in its discretion, may require any State member bank owned or controlled by such affiliate to surrender its stock in the Federal reserve bank and to forfeit all rights and privileges of membership in the Federal reserve system as provided in section 9 of this act.

"Any officer, director, agent, or employee of any such affiliate which has filed an agreement with the Federal Reserve Board, as provided in this section, who shall make any false entry in any book, report, or statement of such affiliate with intent in any case to injure or defraud such affiliate, any member bank or any other company, body politic or corporate, or any individual person, or with intent to deceive any officer of such affiliate or of any member bank, or the Federal Reserve Board, or any agent or examiner appointed to examine the affairs of such affiliate, shall be deemed guilty of a misdemeanor, and upon conviction thereof in any district court of the United States, shall be fined not more than \$5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"No State member bank shall (1) make any loan on the stock of any affiliate which owns or controls such State member bank directly or indirectly, (2) make any loan to any affiliate which owns or controls such State member bank, directly or indirectly, on the security of any shares of stock of any corporation owned or controlled by such affiliate, or (3) be the purchaser or holder of the stock of such affiliate, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and any stock so purchased or acquired shall be sold or disposed of at public or private sale within two years from the date of its acquisition."

Section 21: If the Committee on Banking and Currency decides to recommend the enactment of section 21 of the bill in substantially its present form, it is suggested that paragraph (d) of section 5155 of the Revised Statutes (which forbids the establishment of any branch in a place with a population

of less than 25,000) be amended in order that small communities may not be denied the banking facilities which otherwise might be provided under this section. It is also suggested that the second paragraph of section 9 of the Federal reserve act be amended so as to place State member banks on the same basis as national banks with respect to branches either in this country or in foreign countries.

The sentence commencing in line 7 on page 46 of the bill might be substituted for paragraph (d) of section 5155 of the Revised Statutes; and the following might be added at the end of the second paragraph of section 9 of the Federal reserve act:

"Provided, however, That nothing herein contained shall prevent any State member bank from establishing and operating branches in the United States or any dependency or insular possession thereof or in any foreign country, on the same terms and conditions and subject to the same limitations and restrictions as are applicable to the establishment of branches by national banks."

Section 23: This section is desirable; but, in view of the fact that the Federal reserve act authorizes different rates of discount for different classes of paper, it is recommended that this section be amended by striking out the word "of" in line 2 on page 47 and inserting in lieu thereof the words "on 90-day commercial paper in effect at."

Section 24: While it is recognized that certain evils arise from the competitive bidding for deposits through the payment of undue high rates, it is believed that it is undesirable to further regulate by law the rates of interest, which may be paid on deposits, especially since to do so would place member banks at a disadvantage in competition with nonmember banks. It is, therefore, recommended that this section be omitted.

Section 25: In the interests of clarity, it is recommended that subsection (a) of section 25 of the bill be amended by striking out the period at the end thereof (i. e., at the end of line 8 on page 48) and inserting the following: "in which such corporation owns or controls a majority interest."

It is recommended that the remainder of section 25 of the bill (p. 48, lines 9-25 and p. 49, lines 1-21) be omitted entirely.

The first part of paragraph (b) (lines 9 to 18, inclusive, on page 48) would seem to be unnecessary because the exceptions in section 5200 are not applicable to borrowers of the kind described, except the eighth exception which applies only to loans secured by Government securities.

In so far as the remainder of paragraph (b) and the provisions of paragraph (c) relate to affiliates of national banking associations, the exact meaning of the restrictions is not clear; but these provisions appear to be in conflict with those of section 9 of the bill, and the limitations on loans which may be made by national banking associations to their affiliates are covered adequately by the proposed substitute for section 9. This substitute contains a limitation on loans that may be made to one affiliate and a separate limitation on the aggregate amount of loans that may be made to all affiliates of the same member bank.

In the comments upon the definition of the term "affiliate" in section 2 of the bill certain principles were indicated which have been applied in the recommendations with respect to various sections of the bill relating to affiliates; and it is believed that these recommendations are sufficient.

Section 26: It is recommended that this section be omitted entirely.

It would apply to all loans on "collateral security" regardless of the nature of the security, and would nullify certain provisions of section 5200 of the Revised Statutes, including those permitting national banks to make loans (1) in amounts not exceeding 25 per cent of their capital and surplus on the security of shipping documents or chattel mortgages on live stock, and (2) in amounts not exceeding 50 per cent of their capital and surplus on the security of shipping documents, warehouse receipts, or other such documents covering readily marketable, nonperishable staples. It would greatly curtail the amount of credit which could be extended by banks in agricultural communities to farmers, cattlemen, and dealers in cotton, grain, and other agricultural commodities.

Section 27: In order that reports of affiliates of national banks may be required only when deemed necessary and to clarify the provisions of the bill with respect to such reports, it is recommended that section 27 of the bill be amended to read as follows:

"SEC. 27. Section 5211 of the Revised Statutes of the United States, as amended, is further amended, by adding at the end thereof the following new paragraph:

"Whenever it shall be deemed necessary in order to obtain adequate information regarding the relations between any national bank and its affiliates, or the effect of such relations upon the management or condition of such bank, it may be required under rules and regulations prescribed by the Comptroller of the Currency to obtain and furnish such reports as to any or all of its affiliates as may be called for. Each such report shall contain such information and shall be submitted at such time as may be specified in the call therefor."

Section 28: Section 28 of the bill purports to authorize examinations of affiliates of both national banks and State member banks; but it is doubtful whether it would accomplish this purpose as to State member banks, because it amends the first paragraph of section 5240 of the Revised Statutes so as to provide for such examinations to be made by examiners acting under the jurisdiction of the Comptroller of the Currency, whereas section 9 of the Federal reserve act, as amended by the act of June 21, 1917, exempts State member banks from examination by the Comptroller of the Currency under the provisions of the first two paragraphs of section 5240 of the Revised Statutes. It has been recommended above that section 6 of the bill be amended so as to provide for examinations of affiliates of State member banks; and it is recommended that section 28 of the bill be amended to read as follows:

"SEC. 28. Section 5240 of the Revised Statutes of the United States, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

"Examiners appointed under the provisions of the first paragraph of this section may examine any affiliate of a national bank whenever it shall be deemed necessary in order to obtain adequate information concerning the relations of such affiliate with such national bank or the effect of such relations upon the management or condition of such national bank. The examiner making the examination of any affiliate of a national bank shall have power to make a thorough examination of all the affairs of the affiliate, and in doing so he shall have power to administer oaths and to examine any of the officers and agents thereof under oath and to make a report of his findings to the Comptroller of the Currency. The expense of examinations provided for in this paragraph may be assessed by the Comptroller of the Currency upon the affiliates examined in proportion to assets or resources held by the affiliates upon the dates of examination of the various affiliates. If any such affiliates shall refuse to pay such expenses or shall fail to do so within sixty days after the date of such assessment, then such expenses may be assessed against the affiliated national bank and, when so assessed, shall be paid by such national bank: *Provided, however,* That, if the affiliation is with two or more national banks, such expenses may be assessed against, and collected from, any or all of such national banks in such proportions as the Comptroller of the Currency may prescribe. If any affiliate of a national bank shall refuse to permit an examiner to make an examination of the affiliate or shall refuse to give any information required in the course of any such examination, the national bank with which it is affiliated shall be subject to a penalty of not more than \$100 for each day that any such refusal shall continue. Such penalty may be assessed by the Federal Reserve Board, in its discretion, and, when assessed, may be collected by the Federal reserve bank by suit or otherwise."

Section 29. Section 29 provides for the removal of officers or directors of national banks under certain circumstances. It is believed that there should be some means by which in extreme cases unsatisfactory management could be corrected through the removal of officers and directors responsible therefor.

It is believed, however, that the power of removal should be vested in the Federal Reserve Board as a whole rather than in a special committee consisting of three officials, one of whom is the person bringing the charges against the accused officer or director; and, in order to afford adequate additional protection to the interests of the banks and their officers and directors, certain other changes in this section should be made. It is, therefore, recommended that section 29 be amended to read as follows:

"SEC. 29. Whenever, in the opinion of the Comptroller of the Currency, any director or officer of a national bank, or of a bank or trust company doing business in the District of Columbia, or whenever, in the opinion of a Federal reserve agent, any director or officer of a State member bank in his district, shall have continued to violate any law relating to such bank or shall have

continued unsafe or unsound practices in conducting the business of such bank after having been warned by the Comptroller of the Currency or the Federal reserve agent, as the case may be, to discontinue such violations of law or such unsafe or unsound practices, the Comptroller of the Currency or the Federal reserve agent, as the case may be, may certify the facts to the Federal Reserve Board. In any such case, the Federal Reserve Board may cause notice to be served upon such director or officer to appear before such board to show cause why he should not be removed from office. A copy of such order shall be sent to each director of the bank affected by registered mail. If, after granting the accused director or officer a reasonable opportunity to be heard, the Federal Reserve Board finds that he has continued to violate any law relating to such bank or has continued unsafe or unsound practices in conducting the business of such bank after having been warned by the Comptroller of the Currency or the Federal reserve agent to discontinue such violation of law or such unsafe or unsound practices, the Federal Reserve Board, in its discretion, may order that he be removed from office. A copy of such order shall be served upon such director or officer. A copy of such order shall also be served upon the bank of which he is a director or officer, whereupon such director or officer shall cease to be an officer or director of such bank: *Provided, however,* That such order and the findings of fact upon which it is based shall not be made public or disclosed to any one except to the officer or director involved and the directors of the bank involved, and no such finding or order nor the evidence upon which it is based shall be produced in any court of law except as evidence to punish violations of law under this section. Any such director or officer upon whom any such order has been served as herein provided and who thereafter participates in any manner in the management of such bank shall be fined not more than \$5,000 or imprisoned for not more than five years, or both, in the discretion of the court."

Mr. MEYER. Thank you, Mr. Chairman.

The CHAIRMAN. The next witness is Mr. Pole, the Comptroller of the Currency.

**STATEMENT OF J. W. POLE, COMPTROLLER OF THE CURRENCY,
TREASURY DEPARTMENT, WASHINGTON, D. C.**

Mr. POLE. Mr. Chairman and members of the Banking and Currency Committee; with the permission of the committee, I should like to confine by remarks to those provisions of the bill which affect the office of the Comptroller of the Currency with respect to the responsibilities imposed upon him by law, both in connection with the operation of the national banks and the maintenance of the system of national banks as an instrumentality of the Federal Government. I shall, therefore, pass over without comment those provisions of the bill relating to the Federal reserve system and the use of the facilities of that system by member banks. Although I am a member of the Federal Reserve Board, my responsibility in that connection is shared by the other members. These questions I leave to the board. They have already been discussed by the governor.

I am in sympathy with what I conceive to be the general purpose of this bill, namely, the establishment of a high standard of commercial banking within the Federal reserve system. It seems to me, however, that there are fundamental practical difficulties in the realization of this objective so long as Congress has legislative control over only a portion of the institutions which are engaged in the general banking business. The Federal Government exercises no control whatever over State banks and trust companies operating on the outside of the Federal reserve system. It has control over the banking operations of State member banks of the Federal reserve system only to the extent that it may set up conditions of member-

ship in that system. It may restrict the operation of such member banks; but Congress can not confer upon them charter powers to bring them within a national operating standard, nor can the Federal Government enforce the State laws against such member banks. The third class of banks are the national banks which are wholly under the jurisdiction and control of the Federal Government and are instrumentalities thereof.

Let us assume for the sake of argument that a high standard of banking in the United States would require commercial banks to divorce themselves from all connections with the securities business, the savings bank business, and the trust company business—and I take it that this is, in part, one of the underlying purposes of the bill, particularly with reference to securities: How can Congress make any such standard fully effective if the standards set up for the national banks are more severe than can be enforced upon the State member banks in the Federal reserve system? A national bank can easily escape the higher standard by taking out a State charter and still remain in the Federal reserve system. If Congress attempts to bring the State member bank standard up to the national bank standard through the imposition of conditions upon membership in the Federal reserve system, such State member banks can escape that standard by choosing to operate as State banks on the outside of the Federal reserve system.

In this connection I wish to direct the attention of the committee to the fact that whereas the national banks at one time controlled nearly all of the commercial banking resources of the country, to-day they hold less than half of it. Within the last few years we have witnessed one large bank after another giving up its national charter and taking out a State charter. The motive for thus removing themselves from the direct supervision and control by the Federal Government was undoubtedly to gain, from the standpoint of the bank, more favorable operating conditions. It is true they have remained within the Federal reserve system. New restrictions by Congress applicable solely to national banks must inevitably accentuate this movement from national to State bank charters.

Under such conditions we have to face the question of a Federal Reserve system composed solely of State member banks, with Congress limited in its control over banking operations to setting up conditions of membership in the Federal reserve system. This method of control is too weak to furnish the basis for a national policy in banking. There are two methods of setting up a standard of banking: One is negative by prohibitions upon the exercise of certain powers, and the other is positive by conferring upon banks the appropriate powers to conduct a sound banking business. As to national banks, Congress can legislate with respect to both of these elements, but as to State member banks it is limited to the former and must leave to the State legislatures to confer the positive powers of banking.

Looking at banking from the standpoint of a national question, particularly its essential connection with commerce and industry, it seems to me that the conclusion is inescapable that Congress should, if it can possibly do so, have complete control over the charter powers and the Federal Government complete supervision over the operations of all members of the Federal reserve system, and

should prohibit commercial banking by banks outside of that system. If that be impossible or impracticable of realization, a bill of this character, that is to say, a bill which attempts to raise the standard of banking for national banks alone, will fall short of its purpose because its provisions can be evaded by banks who choose to remove themselves from the jurisdiction of the Federal Government.

There are many sections of this bill which impose what may be regarded as burdens upon national banks but not upon State member banks. This is particularly true of those sections which amend the national bank act, such as restrictions on voting national bank stock, holding company control over national banks, and the divorce of national bank affiliates through prohibition of indorsement on stock certificates of national banks.

Without attempting to submit a complete analysis of the bill, I should like to discuss some of its provisions. In section 14, which amends the law respecting loans upon the security of real estate, there is a provision which makes it mandatory upon the Comptroller of the Currency at the time of each examination of a national bank to revise the appraisal or valuation of all of the real estate upon the security of which a bank may have made loans. Furthermore, the comptroller is given the power to order changes in these loans and to require adjustments to such revised appraisals. Apart from the question of the legality of reducing the amount of a loan after it is made and before it is due, theoretically, this may be considered a sound procedure in that it apparently attempts to provide that such loans shall at all times be properly secured.

The practical difficulty, however, of reappraising twice a year the vast amount of real estate offered as security for loans made by national banks seems to me impossible of realization, since the Comptroller of the Currency has no facilities for making such appraisals and the mere physical performance of the duties imposed by this provision of examining the various parcels of real estate in question could not be achieved during the course of examination of a bank.

Senator GLASS. Apart from the practical operation of a provision of that sort that is precisely what the comptroller does, and every examination with respect to collateral loans, is it not?

Mr. POLE. That is true with regard to collateral loans, sir, except as such collateral may consist of real estate loans.

Senator GLASS. I myself think that the question of practicability is largely involved there.

Mr. POLE. I think so.

There is another clause in this section which classifies as real estate those "unsecured loans whose eventual safety depends upon the value of real estate." The Comptroller of the Currency would have extreme difficulty in attempting to enforce this provision. In my opinion, the language is not susceptible of application to concrete situations and would lead the examiner into all sorts of difficulties, in addition to which the words "whose eventual safety" do not appear to have any definite, technical, legal meaning; but, if I understand the thought, certainly almost any unsecured loan in an agricultural community might eventually depend on real estate. This provision

would unquestionably cause contraction of credit in the agricultural districts.

In view of the fact that in many States there is no savings bank law and national banks in these States receive time deposits it will be necessary for the Comptroller of the Currency under this section of the bill to set up an eligible list of property and securities for investment by national banks of their time deposits. This procedure would put upon the Comptroller of the Currency a considerable burden of responsibility since it necessarily assumes the ability of the comptroller to make a selection which will be safe and sound for investments which deserve the highest protection—an undertaking which at the present moment seems almost too difficult.

There is a provision at the end of section 14 which requires both national and State member banks to comply fully with the provisions of this section. If this compliance as to State member banks is applicable only to that clause of the section requiring such member banks to report their investments to the Federal Reserve Board, then all of the other limitations in the section operate against national banks alone. That is to say, State member banks would not be required to segregate their time deposits and to invest them in real estate and other property and securities listed by the Comptroller of the Currency; but if on the other hand all of the provisions of this section are intended to be made applicable to State member banks, there would seem to be fundamental difficulties in enforcing those provisions which imply supervision by the Comptroller of the Currency, such as reappraisal of real estate and setting up an eligible list for investment of time deposits. Whatever the intention of the section as now drafted, it would seem unfair to national banks to impose limitations upon national banks which can not be and are not imposed upon State member banks.

Section 15 contains a clause which authorizes national banks to engage in all forms of banking business and undertaking all types of banking transactions which the laws of the State in which the national bank is situated permits to State banks, except in so far as there may be a conflict with the Federal statute.

This provision, while apparently designed to enlarge the powers of national banks in order that they may be able to compete with State banking institutions in each State, would not, it seems to me, give to the national banks any advantage worthy of consideration, but, on the other hand, it might permit them to engage in certain inferior phases of banking which would not be desirable. What I have in mind is that the standard of the national banks is, as a rule, higher than that of the State banks, and all of the legitimate forms of banking operations are dealt with in the national banking laws. There is, therefore, nothing left in the field of State bank operations which would be desirable for national banks to have. It is my view that this clause is based upon the wrong principle. It would be in the direction of lowering the standard of the national banks to that of the State banks.

I wish to direct attention also to the great difficulty in supervision the enactment of this provision would cause. In each of the 48 State bank jurisdictions it would be necessary for the Comptroller of the Currency specifically to inform himself of all of those provisions of the State banking law which are not in conflict with the

national bank act, the Federal reserve act, or other Federal statutes and to catalogue them as a part of the national banking powers in each State. It would be necessary for the Comptroller of the Currency to go further and to inform himself accurately of the rules and regulations of the State banking departments interpreting, construing, and applying those laws, and in addition to familiarize himself with the decisions of the State courts to the same effect, otherwise he would not know the exact character and extent of the charter powers of the banks under his supervision. I am not qualified to pass on the purely legal criticism of this provision, but it seems to me that these State laws which may thus be applicable to national banks become, in effect, provisions of the Federal statutes, otherwise how could the Comptroller of the Currency enforce them against the national banks in case of violation? We, therefore, would have, it seems to me, the confusion of enforcing in the Federal courts what were designed by the State legislatures to be applicable only to the local institutions. I see endless complications if this provision becomes a law. There should be no twilight zone in the supervision of the national banks.

There is a provision in this section which repeals the existing law which permits national banks to have bond departments which sell bonds to their customers. This provision, as I understand the bill, is applicable to national banks alone. The repeal of this charter power without a corresponding restriction upon State member banks might cause some national banks to give up their charters in favor of State charters.

I approve of the increase in capital for national banks to a minimum of \$50,000.

Senator GLASS. Why does a national bank ever give up its charter to take a State bank charter?

Mr. POLE. So that it may have, perhaps, greater ease of operation.

Senator GLASS. And engage in unsafe banking?

Mr. POLE. Well, I would perhaps say more liberal banking in a good many instances.

Senator GLASS. You said that there is nothing in the State banking requirements that is soundly available to the national bank.

Mr. POLE. I know of nothing that is desirable in the State law that is not embodied in the national banking law.

Senator GLASS. Then, why should a national bank give up its charter and go into the State bank business?

Mr. POLE. Greater liberality of powers, sound or unsound.

Senator GLASS. And chiefly unsound, do you think?

Mr. POLE. I would not say so, Senator.

Senator GLASS. I know; but you think so, do you not?

Mr. POLE. I can not think out loud, sir. [Laughter.]

The CHAIRMAN. I might ask at this time: You say quite a number of national banks take State charters. Is the reverse true in a good many instances?

Mr. POLE. Not comparable at all to the number of banks which have gone out of the system over the period of recent years.

Senator FLETCHER. You mean more have gone out than have come in.

Mr. POLE. Many more have gone out than have come in.

Senator WALCOTT. Have you any idea of the flight of capital from the Federal reserve system to the member systems?

Mr. POLE. It has increased, Senator, but I have not the figures here. If you would like to have them I would be glad to put them in the record.

Senator WALCOTT. It would be an interesting exhibit to put in the record, going back over a period of five years by years.

Mr. POLE. Five years by years, giving the amount of capital increase in member banks.

Senator WALCOTT. At the expense of the Federal reserve system. That gives the amount of capital that has disappeared, flown from the Federal reserve system and taken up State charters.

Senator BULKLEY. You mean national banking system, do you not?

Senator WALCOTT. Yes.

Mr. POLE. From the national banking system, yes.

Senator WALCOTT. That is the Federal reserve system.

Senator GLASS. There are many State banks that are in the Federal reserve system.

Senator WALCOTT. I am not talking about the national banks; I am talking about the Federal reserve system.

Mr. POLE. Yes.

Senator WALCOTT. That is what you are talking about; you are talking about the national?

Mr. POLE. I am talking about the national system, yes.

Mr. WALCOTT. I am anxious to know how many banks have escaped from the Federal reserve system. You have that, do you?

Mr. POLE. Yes.

Senator WALCOTT. I would like that, and then I would like also the banks that have gone out of the national and become State banks.

Mr. POLE. State member banks?

Senator WALCOTT. State member banks; yes, sir.

Mr. POLE. And State nonmember banks. Yes, I will furnish that.

Senator GLASS. Ten years ago, as I recall, approximately the total assets of the banks in the Federal reserve system, not simply the national banks, but the banks in the Federal reserve system, were about 70 per cent of the total banking assets of the country, as against about 30 per cent in the State banking system. But that has been quite much changed in recent years.

Mr. POLE. Yes, it has, Senator.

Senator WALCOTT. Has there been any movement, do you think, from nonmember to member banks, any increase in membership?

Mr. POLE. Some slight movement.

Senator WALCOTT. Very slight?

Mr. POLE. Yes.

Senator WALCOTT. But more than there have been withdrawals?

Mr. POLE. Banks which have gone out of the system?

Senator WALCOTT. Yes.

Mr. POLE. I should think not, Senator.

Senator WALCOTT. That is what I want to see.

Mr. POLE. Yes. I will say that the Federal reserve system is not losing net resources.

Senator WALCOTT. That is the picture that I want to get accurately.

(Hereafter Mr. Pole submitted for the record the following data and tables:)

COMPTROLLER OF THE CURRENCY,
Washington, D. C., April 14, 1932.

HON. PETER NORBECK,
Chairman Banking and Currency Committee,
United States Senate, Washington, D. C.

DEAR MR. CHAIRMAN: In accordance with request of the committee, I am sending you herewith:

(1) A table showing, by years, for the 10-year period beginning November 1, 1921, and ending October 31, 1931, the number of national banks, with capital, which have entered the State banking systems.

(2) A table showing for the 10-year period given in Table No. 1, by number and capital, the State banks which had converted into national banks.

(3) A table showing by names, capital and total resources, 152 national banks, with resources of over \$5,000,000 each, which have left the national banking system for the 12-year period beginning 1920.

Information with respect to the State banks which have become State members of the Federal reserve system or have withdrawn as State members is not available.

Very truly yours,

J. W. POLE, Comptroller.

TABLE No. 1.—Number and capital of national banks which went into voluntary liquidation and converted into State banks in the 10 years ended October 31, 1931

Year ended Oct. 31—		Number of banks	Authorized capital	Year ended Oct. 31—Con.	
1922	77	\$12,590,000	1923	99	21,835,000
1923	73	30,070,000	1924	139	91,672,500
1924	96	24,165,000	1925	148	28,622,900
1925	71	10,055,000	1930	135	28,945,000
1926	92	18,923,300	1931		
1927	99	28,170,000	Total	1,029	293,048,700

TABLE No. 2.—Number and capital of national banks chartered which were conversions of State banks in the 10 years ended October 31, 1931

Year ended Oct. 31—		Number of banks	Authorized capital	Year ended Oct. 31—Con.	
1922	129	\$13,815,800	1923	25	11,260,000
1923	69	11,192,500	1924	23	7,620,000
1924	29	6,055,000	1930	31	3,040,000
1925	86	10,235,000	1931	6	700,000
1926	29	9,380,000	Total	457	101,608,300
1927	30	28,310,000			

List of 152 large national banks which have within the past 12 years given up their national charters for the purpose of operating under State charters

Name and location of bank	State	Capital	Resources
Year ended Oct. 31, 1927			
American Exchange-Pacific National Bank of New York	New York	\$7,500,000	\$264,212,000
First National Bank of Albany	do	600,000	15,154,000
West Branch National Bank of Williamsport	Pennsylvania	800,000	9,637,000
Citizens National Bank & Trust Co. of Cincinnati	Ohio	2,000,000	20,337,000
Fifth-third National Bank of Cincinnati	do	3,000,000	53,527,000
Merchants & Manufacturers National Bank of Newark	New Jersey	1,350,000	20,458,000
Commercial National Trust & Savings Bank of Los Angeles	California	2,000,000	25,118,000
Griswold National Bank of Detroit	Michigan	2,000,000	22,733,000
American National Bank of Newark	New Jersey	500,000	17,662,000
Franklin National Bank of New York	New York	800,000	7,283,000

List of 152 large national banks which have within the past 12 years given up their national charters for the purpose of operating under State charters—Continued.

Name and location of bank	State	Capital	Resources
<i>Year ended Oct. 31, 1928</i>			
Union National Bank of Philadelphia.....	Pennsylvania.....	\$1,000,000	\$23,044,000
City National Bank of Holyoke.....	Massachusetts.....	500,000	5,803,000
National Bank of Commerce in Chicago.....	Illinois.....	800,000	7,717,000
National Bank of Commerce in Philadelphia.....	Pennsylvania.....	500,000	10,732,000
Hamilton National Bank of New York.....	New York.....	1,500,000	19,216,000
Bronx National Bank of the City of New York.....	do.....	300,000	9,986,000
First National Bank of Bangor.....	Maine.....	400,000	8,308,000
Liberty National Bank of Covington.....	Kentucky.....	350,000	5,676,000
First National Bank of Columbus.....	Ohio.....	500,000	14,071,000
Massasoit-Pocasset National Bank of Fall River.....	Massachusetts.....	650,000	6,752,000
United Capitol National Bank & Trust Co. of New York.....	New York.....	5,000,000	53,144,000
Flushing National Bank, Flushing.....	do.....	200,000	5,070,000
National Bank of Rochester.....	do.....	1,200,000	22,583,000
Broad Street National Bank of Philadelphia.....	Pennsylvania.....	500,000	12,293,000
National Bank of North Philadelphia.....	do.....	700,000	6,872,000
National City Bank of Los Angeles.....	California.....	1,000,000	10,898,000
<i>Year ended Oct. 31, 1929</i>			
First National Bank of Brooklyn.....	New York.....	1,000,000	23,025,000
Seventh National Bank of New York.....	do.....	1,500,000	14,524,000
American National Bank of Richmond.....	Virginia.....	2,000,000	21,774,000
Merchants National Trust & Savings Bank of Los Angeles.....	California.....	4,000,000	164,045,000
Northern National Bank of Philadelphia.....	Pennsylvania.....	400,000	10,256,000
National Union Bank of Maryland at Baltimore.....	Maryland.....	1,000,000	11,032,000
Mercantile National Bank in Dallas.....	Texas.....	1,000,000	13,950,000
First National Bank of Long Beach.....	California.....	200,000	6,916,000
National Bank of Commerce in New York.....	New York.....	25,000,000	684,456,000
First National Trust & Savings Bank of Whittier.....	California.....	250,000	7,639,000
Bloomfield National Bank, Bloomfield.....	New Jersey.....	300,000	7,457,000
Old National Bank of Grand Rapids.....	Michigan.....	800,000	16,666,000
Nanover National Bank of the City of New York.....	New York.....	10,000,000	209,026,000
Third National Bank of Syracuse.....	do.....	300,000	5,508,000
Liberty National Bank & Trust Co. of Syracuse.....	do.....	400,000	5,002,000
Chemical National Bank of New York.....	do.....	6,000,000	233,708,000
Chapman National Bank of Portland.....	Maine.....	400,000	9,750,000
Louisville National Bank & Trust Co., Louisville.....	Kentucky.....	750,000	14,679,000
Merchants National Bank of Detroit.....	Michigan.....	2,000,000	26,780,000
Arcadia National Bank & Trust Co. of Newark.....	New York.....	200,000	5,866,000
Seaboard National Bank of the City of New York.....	do.....	11,000,000	286,954,000
Merchants-Laclede National Bank of St. Louis.....	Missouri.....	1,700,000	23,751,000
State National Bank of St. Louis.....	do.....	2,000,000	21,667,000
Tenth National Bank of Philadelphia.....	Pennsylvania.....	1,000,000	10,746,000
Community National Bank of Buffalo.....	New York.....	1,000,000	23,596,000
Fordham National Bank in New York.....	do.....	500,000	5,616,000
Thamet National Bank, Norwich.....	Connecticut.....	1,000,000	5,218,000
Norwood National Bank.....	Ohio.....	200,000	5,157,000
City National Bank of San Antonio.....	Texas.....	1,000,000	14,040,000
National City Bank of Akron.....	Ohio.....	1,000,000	15,461,000
National Bank of Niagara & Trust Co., Niagara Falls.....	New York.....	1,200,000	13,492,000
Citizens National Bank of Raleigh.....	North Carolina.....	750,000	8,679,000
Murchison National Bank of Wilmington.....	do.....	1,000,000	12,285,000
American National Bank & Trust Co. of Greensboro.....	do.....	1,000,000	11,297,000
City National Bank & Trust Co. of Bridgeport.....	Connecticut.....	1,000,000	18,351,000
<i>Year ended Oct. 31, 1920</i>			
Third National Bank of Atlanta.....	Georgia.....	1,000,000	27,053,000
Marchants National Bank of the City of New York.....	New York.....	3,000,000	49,942,000
Security National Bank of Los Angeles.....	California.....	600,000	8,353,000
Farmers National Bank of Fresno.....	do.....	300,000	6,985,000
Mercantile National Bank of San Francisco.....	do.....	2,000,000	20,224,000
<i>Year ended Oct. 31, 1921</i>			
National Reserve Bank of Kansas City.....	Missouri.....	1,000,000	11,534,000
Midwest National Bank & Trust Co. of Kansas City.....	do.....	1,000,000	12,542,000
Lincoln National Bank of Rochester.....	New York.....	1,000,000	22,272,000
First National Bank of Cleveland.....	Ohio.....	2,500,000	101,524,000
Union National Bank of Newark.....	New Jersey.....	1,500,000	31,372,000
Union Commerce National Bank of Cleveland.....	Ohio.....	4,000,000	78,323,000
Canal-Commercial National Bank of New Orleans.....	Louisiana.....	500,000	11,863,000
National Bank of Commerce of Toledo.....	Ohio.....	1,000,000	16,781,000
Central National Bank of St. Louis.....	Missouri.....	1,000,000	27,629,000
National Commercial Bank of Cleveland.....	Ohio.....	1,500,000	14,768,000
Liberty National Bank of New York.....	New York.....	5,000,000	121,642,000
National Bank of Commerce of Kansas City.....	Missouri.....	4,000,000	68,613,000
Union National Bank of Pasadena.....	California.....	375,000	5,404,000
Ridgewood National Bank, Ridgewood.....	New York.....	300,000	9,224,000
National Bank & Trust Co. of Pasadena.....	California.....	300,000	6,490,000

List of 152 large national banks which have within the past 12 years given up their national charters for the purpose of operating under State charters—Continued.

Name and location of bank	State	Capital	Resources
<i>Year ended Oct. 31, 1923</i>			
First National Bank of Fresno.....	California.....	\$500,000	\$9,771,000
First National Bank of Berkeley.....	do.....	300,000	6,717,000
First National Bank of Bakersfield.....	do.....	400,000	7,127,000
Atlantic National Bank of the City of New York.....	New York.....	1,000,000	21,776,000
Bank of New York National Banking Association.....	do.....	2,000,000	76,135,000
National State & City Bank of Richmond.....	Virginia.....	1,000,000	15,854,000
<i>Year ended Oct. 31, 1923</i>			
Merchants National Bank of San Diego.....	California.....	250,000	5,108,000
Lowry National Bank of Atlanta.....	Georgia.....	1,000,000	21,350,000
Irving National Bank, New York.....	New York.....	12,500,000	297,935,000
Bank of North America, Philadelphia.....	Pennsylvania.....	2,000,000	31,490,000
Merchants National Bank of San Francisco.....	California.....	1,500,000	15,032,000
First-Second National Bank of Akron.....	Ohio.....	1,500,000	22,603,000
Importers and Traders National Bank of New York.....	New York.....	1,500,000	43,550,000
Merchants National Bank of Raleigh.....	North Carolina.....	300,000	5,576,000
Luzerno County National Bank of Wilkes-Barre.....	Pennsylvania.....	400,000	5,018,000
Battery Park National Bank of New York.....	New York.....	1,500,000	12,982,000
American National Bank of San Francisco.....	California.....	2,000,000	25,623,000
Ninth National Bank of Philadelphia.....	Pennsylvania.....	500,000	14,527,000
<i>Year ended Oct. 31, 1924</i>			
Fourth National Bank of Cincinnati.....	Ohio.....	500,000	12,418,000
Wells Fargo National Bank of San Francisco.....	California.....	6,000,000	93,806,000
National Exchange Bank of Baltimore.....	Maryland.....	1,500,000	17,532,000
Lafayette National Bank of Buffalo.....	New York.....	1,000,000	9,128,000
Continental National Bank & Trust Co. of Kansas City.....	Missouri.....	500,000	6,499,000
Northern National Bank of Toledo.....	Ohio.....	1,000,000	15,692,000
Long Beach National Bank, Long Beach.....	California.....	200,000	7,415,000
Second National Bank of Toledo.....	Ohio.....	1,000,000	16,477,000
Corn Exchange National Bank of Chicago.....	Illinois.....	5,000,000	132,302,000
<i>Year ended Oct. 31, 1925</i>			
First National Bank of Oakland.....	California.....	1,000,000	11,953,000
Fifth National Bank of the City of New York.....	New York.....	1,200,000	25,302,000
Gotham National Bank of New York.....	do.....	1,500,000	19,371,000
National Union Bank of Boston.....	Massachusetts.....	1,000,000	17,129,000
<i>Year ended Oct. 31, 1926</i>			
Manufacturers & Traders National Bank of Buffalo.....	New York.....	2,000,000	61,935,000
Coal & Iron National Bank of the City of New York.....	do.....	1,500,000	25,778,000
First National Bank of Hammond.....	Indiana.....	250,000	5,433,000
Planters National Bank of Richmond.....	Virginia.....	1,000,000	17,647,000
Norwood National Bank of Greenville.....	South Carolina.....	250,000	7,085,000
National Exchange Bank of Providence.....	Rhode Island.....	1,250,000	20,871,000
First National Bank of Jamaica.....	New York.....	200,000	9,862,000
City National Bank of Plainfield.....	New Jersey.....	150,000	7,195,000
State National Bank of North Tonawanda.....	New York.....	600,000	8,007,000
Phoenix National Bank of Hartford.....	Connecticut.....	1,000,000	17,714,000
National Exchange Bank of Lockport.....	New York.....	700,000	6,655,000
Second National Bank of Hoboken.....	New Jersey.....	300,000	6,653,000
First National Bank & Trust Co. of Utica.....	New York.....	1,250,000	19,821,000
National American Bank of New York.....	do.....	1,000,000	12,376,000
National Butchers & Drovers Bank of the City of New York.....	do.....	2,000,000	14,447,000
<i>Year ended Oct. 31, 1930</i>			
Textile National Bank of Philadelphia.....	Pennsylvania.....	500,000	7,413,000
Peoples-First National Bank of Charleston.....	South Carolina.....	1,000,000	10,573,000
City National Bank & Trust Co. of Dayton.....	Ohio.....	750,000	19,550,000
Exchange National Bank of Little Rock.....	Arkansas.....	400,000	5,674,000
Kalamazoo National Bank & Trust Co. of Kalamazoo.....	Michigan.....	500,000	5,725,000
National Bank of Baltimore.....	Maryland.....	1,500,000	20,756,000
North Ward National Bank of Newark.....	New Jersey.....	400,000	14,404,000
National City Bank of St. Louis.....	Missouri.....	1,000,000	12,900,000
Central National Bank of the City of New York.....	New York.....	2,500,000	15,410,000
Utica National Bank & Trust Co. of Utica.....	do.....	750,000	6,706,000
National Security Bank & Trust Co. of Philadelphia.....	Pennsylvania.....	400,000	13,040,000
American National Bank & Trust Co. of Mount Vernon.....	South Carolina.....	500,000	8,378,000
Peoples National Bank of Elizabeth.....	New York.....	600,000	8,730,000
Farmers & Merchants National Bank, Baltimore.....	New Jersey.....	300,000	8,171,000
Drovers & Mechanics National Bank, Baltimore.....	Maryland.....	850,000	9,806,000
Broadway National Bank & Trust Co. of New York.....	do.....	1,000,000	20,410,000
Chester National Bank of Chester.....	New York.....	2,000,000	8,411,000
	Pennsylvania.....	300,000	5,437,000

List of 152 large national banks which have within the past 12 years given up their national charters for the purpose of operating under State charters—Continued.

Name and location of bank	State	Capital	Resources
<i>Year ended Oct. 31, 1931</i>			
Dallas National Bank of Dallas.....	Texas.....	\$500,000	\$5,588,000
First National Bank of Davenport.....	Iowa.....	400,000	5,805,000
Seward National Bank & Trust Co. of New York.....	New York.....	2,000,000	7,378,000
American National Bank of Jamestown.....	do.....	300,000	6,055,000
Straus National Bank & Trust Co. of New York.....	do.....	2,000,000	13,570,000
National Bank of the Republic of Chicago.....	Illinois.....	11,000,000	137,856,000
Engineers National Bank of Cleveland.....	Ohio.....	1,000,000	10,864,000

Recapitulation by years of 152 banks	Number	Capital	Resources
1920.....	5	\$6,000,000	\$112,562,000
1921.....	15	24,975,000	539,978,000
1922.....	6	5,200,000	137,380,000
1923.....	12	24,050,000	500,794,000
1924.....	9	16,700,000	310,956,000
1925.....	4	4,700,000	73,755,000
1926.....	15	13,460,000	241,582,000
1927.....	10	20,250,000	456,112,000
1928.....	16	15,100,000	222,230,000
1929.....	35	82,860,000	1,066,789,000
1930.....	18	14,950,000	195,504,000
1931.....	7	17,200,000	196,184,000
Total.....	152	247,225,000	4,952,836,000

Mr. POLE. Yes. Shall I go on?

The CHAIRMAN. These interruptions are only by your permission.

Mr. POLE. That is all right, Senator. I am very glad to have you conduct the hearing in any way you want to.

In the matter of the divorce of security affiliates of national banks by making unlawful the indorsement on the national bank certificate and unlawful also the trust agreement conditioning the sale, it seems to me that a distinction should be made between affiliates engaged in the business of buying and selling investment securities and other corporations not primarily concerned at all in the securities business. The attention of the committee is directed to the fact that this provision is a restriction upon the affiliates of national banks alone and has no application to State member banks.

Section 18: This section so far as national banks are concerned is supplementary to section 17 in that it prevents an interlocking of personnel with an affiliate. It is, however, applicable to both national and State member banks. In my opinion, the language, especially of subsection "C" where the term "a corporation organized for any purpose whatsoever" appears, is too broad. It would apparently embrace banks and trust companies, which, I feel sure, is not intended by the bill.

Section 19: This section denies the right of a shareholder of a national bank to vote unless he actually owns the stock and has acquired it through bona fide purchase, gift or inheritance. There may be other ways of becoming a bona fide owner of bank stock, such as by exchange or by stock dividends, in which case such a shareholder could not vote under this bill. This section also denies

the right to any owner of more than 10 per cent of any national bank stock to vote the same at all unless he be an individual or complies with the provisions of section 20 of the bill. The committee doubtless has given consideration to the disfranchisement of stockholders of national banks which happen to be corporations, associations, or partnerships, but which have no interest in operating a chain of a group of banks.

Senator GLASS. Why haven't they an interest if they own considerable stock in the bank?

Mr. POLE. Senator, there might be stockholders who are steel and industrial corporations, trust companies, banks, and all manner of corporations which might own more than a 10 per cent interest in a bank.

Senator GLASS. They are interested in the operation of the bank?

Mr. POLE. Yes; but they can not vote if they have more than 10 per cent of the stock unless they comply with a number of the provisions which are set out in section 20 of the bill.

Senator GLASS. That is a rare incident in banking business?

Mr. POLE. Not at all, Senator. Not rare; not so rare.

Senator GLASS. You mean the steel corporations and the other corporations are acquiring ownership of banks?

Mr. POLE. And a great many savings banks.

Senator GLASS. All right; go ahead.

Mr. POLE. Attention is particularly directed to the fact that this section is a restriction upon national bank members of the Federal reserve system only and does not apply to State member banks. This is true also of section 20, which places restrictive regulations and reserve requirements upon group bank holding companies which have national banks in their groups. These two sections as they stand would undoubtedly lead to the withdrawal of the great volume of resources now held by national banks in group bank organizations from the national system for the simple reason that any such group organization can escape these burdens by becoming a State bank and still remain within the Federal reserve system.

Senator GLASS. You think that group banking is a wholesome system of banking then, do you?

Mr. POLE. I have never been in favor of it, Senator, except that, as I have said, before it is legislated against, some provision should be made for that large amount of capital which is invested in group banking, and that group banking has been extremely beneficial in a number of sections of this country.

Section 21 contains the branch banking provisions of the bill, but permits national banks to establish branches only in those States where the State law permits it and only to the extent permitted by such State law except for the proviso for a 50-mile extension beyond State lines in certain cases. In my judgment, this section will accomplish little or nothing in the way of branch banking, since only a few States permit state-wide branch banking. The particular need for branch banking by national banks is in those States which do not permit branch banking to the State banks. There is a crying need for banking facilities which can be given by strong city banks in the rural communities of the United States. I know of no other sound solution of the rural bank question.

I need not dwell upon this matter since I have expressed my views at length both before this committee and before the House Committee on Banking and Currency, but I may add that subsequent events have only confirmed me in the recommendations I made for wider branch-banking facilities, in my reports to Congress for the years 1929, 1930, and 1931.

I wish to call the attention of the committee to the fact that the provisions in section 25 amending section 5200 of the Revised Statutes restricting loans to securities dealers, and so forth, apply as restrictions only upon national banks and do not restrict State member banks.

With respect to the provisions of section 27 which provides for an examination by the Comptroller of the Currency of affiliates of national banks, attention is directed to the requirement for publication of the portfolio of such affiliate as a penalty for excessive borrowing from any bank but no corresponding requirement for publication is contained in section 9 requiring the report of the affiliates of State member banks to the Federal Reserve Board.

I most heartily approve of section 29, which provides for the removal of bank officers for persistent violation of law or continued unsound banking practices. I think the mere granting of this power to the reserve system and the Comptroller of the Currency will be sufficient to make unnecessary the exercise of it and will have a wholesome effect upon the whole field of governmental supervision over members of the Federal reserve system.

That concludes my statement, Mr. Chairman.

The CHAIRMAN. Thank you, Mr. Pole. Do any members of the committee want to ask any questions?

Senator GLASS. I do not.

Senator BROOKHART. Yes; I do. You mentioned the matter of credit in the agricultural districts. I found in my State and in Illinois and Indiana and several other States, in the agricultural sections, that the national-bank examiners for many years have been cautioning banks against loans to farmers; said to them, "They are not liquid." Was that a general policy of your department?

Mr. POLE. I would say by no means, Senator. We must always remember that a bank has two classes of customers, depositors and borrowers. The depositors, for the most part, put their money in banks on demand, and if that money is loaned out on slow assets, and unusual demands are made it becomes impossible for the banks to liquidate their loans fast enough to meet that demand. Therefore, it is necessary that a bank should confine certain of its investments to more liquid securities than farm loans.

Senator BROOKHART. Then you did caution against the agricultural loans in that way, some of your bank examiners?

Mr. POLE. No. The examiners have that general knowledge that a bank must have a certain ratio of liquidity; no general instructions to that effect.

Senator BROOKHART. Well, there was a general caution against loans to farmers; that is, for production purposes also?

Mr. POLE. I know of nothing like that, Senator. I do not think you can have any concrete evidence of the existence of any such regulation as that.

Senator BROOKHART. I can bring you some concrete evidence of it, and plenty of it, that it was done by the examiners and quite generally. For instance, one of the best known bankers of my State was cautioned by the national bank examiner against loans to farmers to such an extent that he finally told the examiner to go to hell, and at the same time went ahead with his farm loans. All the time the bank examiner was approving the investment in these listed bonds from New York—that was good banking. He bought about \$125,000 of these bonds, which was not much for his bank, considering the size of it. But after he bought these bonds they depreciated, as all the other bonds did, more than the farmers' paper did. Then the bank examiners came around demanding that he charge off those bonds or set up a reserve against them, and he told them to go to hell again. Now, I know that instance.

Senator GLASS. He must have gone to school with that New York banker that told the Federal Reserve Board to go to hell.

Senator BROOKHART. That is only one of many instances that were brought to my attention. And how many banks failed with frozen farmers' assets?

Mr. POLE. Well, of course, all the country banks have more or less of it.

Senator BROOKHART. Four or five thousand of them?

Mr. POLE. Yes.

Senator BROOKHART. And then later the frozen assets were these listed bonds.

Mr. POLE. That is perfectly true.

Senator BROOKHART. And for a time banks were closed on that.

Mr. POLE. A great many banks have been affected through the depreciation in bonds.

Senator BROOKHART. Then you did approve the investment in those listed bonds everywhere?

Mr. POLE. Well, Congress did that, not we.

Senator BROOKHART. What did Congress say about it? What law was that?

Mr. POLE. Section 2136, in giving national banks the right to invest in securities of a certain character.

Senator BROOKHART. Congress did not express any preference for those over loans to farmers, though, did it?

Mr. POLE. No.

Senator GLASS. That was the amendment in the McFadden bill to section 5136?

Mr. POLE. Yes.

Senator GLASS. It is right interesting to me that the State of the Senator who was most vehement in favor of that suffered almost the entire collapse of its banking system.

The CHAIRMAN. May I ask what was your attitude, the attitude of your department, toward that legislation when it was pending, the McFadden bill?

Mr. POLE. We were in favor of it. As a matter of fact, it was really legalizing something which had already been engaged in.

Senator GLASS. Legalizing a bad practice that had already been engaged in, was it not?

Mr. POLE. That practice, Senator.

The CHAIRMAN. As I recall, a good many Members of the Senate voted for the bill because they thought you recommended it; I mean your department.

Mr. POLE. I do not know whether our department had very much to do with that.

Senator GLASS. And hundreds of banks have failed because of it, have they not, recently, in the last two years?

Mr. POLE. Hundreds of banks, Senator, have been very materially affected by it.

Senator GLASS. Yes.

Senator BROOKHART. Now, the destruction of these banks because of frozen farmers' paper creates this demand for branch banks that you recommend in those communities?

Mr. POLE. Not at all. I should say that the branch banks would probably made more judicious loans, but not necessarily more restrictive where credit was warranted.

Senator BROOKHART. Has not this restrictive policy had about as much to do as anything else with reducing farm prices and land values and bringing about agricultural depression long ahead of the other depression?

Mr. POLE. You are assuming something that does not exist, Senator, when you speak of restrictive policy. There is no restrictive policy by the comptroller's office. There has been a most lenient policy, probably too lenient in a great many instances.

Senator GLASS. Certainly so, is it not?

Mr. POLE. That is certainly so.

Senator BROOKHART. I would like to see what you call restrictive then, see what it would look like. There was 55 years when there was not any of these restrictions or troubles for farmers to get loans. Farmers' paper was the best the banks could get.

Mr. POLE. Yes.

Senator BROOKHART. And then this lenient policy of yours came along and the farmer can not get anything and five thousand of his banks have been closed because of his frozen paper.

Mr. POLE. Senator, I can assure you that the comptroller's office has gone just as far in that direction as it can with safety, having in mind the interests of the creditors of the banks. We must not forget them.

Senator BROOKHART. Well, you have ruined the depositors in the banks by closing the banks too. If the farmers had been able to pay, why, there would have been no trouble with the depositors getting their money.

Mr. POLE. Senator, I will have to differ with you on that. We closed very few banks. They closed themselves. The depositors closed them. Very few banks the comptroller's office closed. We encourage them in every way and do anything we can to keep them from closing, even to going up to the Reconstruction Corporation.

Senator BROOKHART. That is a new thing, the Reconstruction Corporation.

Mr. POLE. That is a new thing; but when the Reconstruction Corporation was not there, we went to the Federal Reserve Bank with them or to their correspondents. We acted as doctors and wet nurses for them.

Senator BROOKHART. But they closed just the same?

Mr. POLE. They closed themselves.

Senator TOWNSEND. I recall some of the witnesses who testified here and indicated that any legislation of this time might be detrimental to the banking interests of the country. What is your judgment on that?

Mr. POLE. I think decidedly to the contrary; that it would be extremely helpful at this time. In fact, I should say that if Congress would amend this provision of Section 21, I think it is, which has to do with branch banking, leaving the section just as it is, with the amendment "regardless of whether or not the States permit it," it would enable the strong banks to give relief and extend their facilities to the rural communities, which would be of invaluable assistance to the country.

Senator GLASS. Are you satisfied, Mr. Pole, that the decisions of the courts certainly make that constitutional?

Mr. POLE. I have been so advised, Senator.

Senator GLASS. I put into the record when we had the prolonged hearings last year a summary of court decisions prepared and given to me by Mr. Collins, formerly deputy comptroller, and I would judge from this summary that it would be entirely within the province of Congress to authorize state-wide branch banking regardless of the laws of the States.

Mr. POLE. I have been advised so by what I regard as first-class authority.

Senator GLASS. But you can not give us any guarantee that Congress would accept our view of it, can you?

Mr. POLE. I am afraid I can not do that. I think we could make an effort, however.

Senator GLASS. As well organized as the effort has been to tear this bill down?

Mr. POLE. I think there is a lot of support for that kind of legislation, because there are a great many thinking people who realize that something has to be done for the banking system, something more than this. We have to protect the rural communities. That is what we are not doing now.

Senator GLASS. I am very sorry you were not a tutor at the night school, because all of the testimony that we have heard here except Governor Meyer today has been to the effect that it would be a fearful thing to enact any legislation at all at this particular time.

Mr. POLE. I think it would be a very good thing. I am not saying there should be any disturbing or drastic legislation, but I do say legislation of proper character would be immensely helpful.

Senator TOWNSEND. Do you agree with the recommendations as made by Governor Meyer?

Mr. POLE. There were no recommendations made with respect to branch banking in that bill, Senator.

Senator TOWNSEND. With the recommendations that he made here?

Mr. POLE. I am a member of the board and subscribed to those recommendations.

Senator GLASS. Then it is no use to catechize you on any particular one of them?

Mr. POLE. No. Those recommendations represent, my views.

Senator GLASS. You had some differences in the board and reconciled them?

Mr. POLE. Yes. There was much argument.

The CHAIRMAN. A pretty good conclusion reached in most of it?

Mr. POLE. In the main I was quite satisfied. That is the kind of night school we have been to.

The CHAIRMAN. It is a different one from the one that we heard about.

Mr. POLE. A little different, I imagine.

Senator GLASS. You did not decide one hour that you did not understand the bill at all and the next hour were so confident that you thoroughly understood it that you deluged the country with telegrams to kill it, did you?

Mr. POLE. No; we did not send out many telegrams, Senator; not any, in fact. We thought there was enough interest in the bill.

The CHAIRMAN. If you have concluded your statement and there are no further questions to be asked by members of the committee, we will conclude the hearings for the day and meet in the room of the Banking and Currency Committee to-morrow we will conclude the hearings on this bill.

(Accordingly, at 5:30 o'clock p. m., the committee adjourned, to meet at 10.30 o'clock a. m. of the next day, Wednesday, March 30, 1932, in committee room, 303 Senate Office Building.)

OPERATION OF THE NATIONAL AND FEDERAL RESERVE BANKING SYSTEM

WEDNESDAY, MARCH 30, 1932

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10.30 o'clock a. m. in room 303, Senate Office Building, pursuant to adjournment on yesterday, Senator Peter Norbeck, presiding.

Present: Senators Norbeck (chairman), Brookhart, Goldsborough, Townsend, Walcott, Fletcher, Glass, Wagner, Barkley, Bulkley, and Costigan.

The CHAIRMAN. The committee will come to order.

Senator GOLDSBOROUGH. Mr. Chairman, if it is in order, I should like to present for the record at this time the following telegram [reading]:

BALTIMORE, Md., *March 22, 1932.*

PHILLIPS LEE GOLDSBOROUGH,
Senate Office Building:

At a meeting held this date of all members of Federal reserve system in Baltimore, it was the unanimous opinion that the enactment of the proposed Glass bill is most inadvisable and highly undesirable at this time.

CHARLES E. RIEMAN,
President Baltimore Clearing House.

Also a letter from Charles E. Rieman, president of the Western National Bank of Baltimore [reading]:

MARCH 22, 1932.

Senator PHILLIPS LEE GOLDSBOROUGH,
United States Senate, Washington, D. C.

DEAR SENATOR GOLDSBOROUGH: There is so much in the bill introduced by Senator Glass, of Virginia, as a revised edition of his earlier bill Senate 4115 that it is impossible to thoroughly trace out its consequences if enacted, so I can only attempt to present some of the salient features for your consideration.

I wish to say, however, that this afternoon I called a meeting of the banks in Baltimore, which are members of the Federal reserve system, and the provisions of the bill were reviewed, with the result that, by unanimous opinion, it was held that it would be ill advised and undesirable to enact the bill at this time. I am inclosing you a copy of the resolution.

Every phase of banking is sensitive enough now without imposing regulation by statute on banking practices, which are part of our national development and sound if not overdone or abused, but, when entirely prohibited by law, destroys the exercise of good judgment so needed to extricate the banking situation from its present condition. I refer to the new limitations on loans to the public and accommodations from the reserve banks; and, further, the drive in the bill against loans secured by stocks and bonds will surely depress the market for securities, if it becomes law. No matter what the ultimate aim of the provisions of the bill may be, values and credits are too sensitive

now to attempt radical regulations in our banking practices. (This does not preclude constructive legislation.)

To refer specifically to the bill, I wish to say first that I have always admired Senator Glass in his determined stand for protection of the Federal reserve system, but he now offers numerous amendments to the Federal reserve act to use the Federal reserve system to correct evils which have been practiced by some member banks, but many have not. The bill contains no provisions to encourage membership in the Federal reserve system or check the tendencies which lead to loss in membership. From March, 1929, to December 31, 1931, the system lost 1,500 member banks, and if I am not greatly mistaken some of the regulations in the proposed act will accelerate the loss in membership and resources.

All that part of the bill dealing with affiliates appears very complete to render them harmless, but it may be better simply to prohibit member banks from having affiliates at some future date when the country emerges from this present depression.

The amendment to the Federal reserve act by inserting the new section 12-B, which creates the Federal liquidating corporation, I believe to be a very unwise provision. Such a corporation as it creates should not be incorporated into the Federal reserve system, and there are many provisions in connection with this that certainly are very undesirable on the part of well managed member banks.

Section 24 regulates the amount of interest to be paid on deposits and this will absolutely work against the best interests of member banks. While the rates allowed appear to be ample at this time, yet the competition between State bank institutions and member banks have savings departments which pay over 3 per cent interest, and if the rate were cut to 3 per cent, millions of deposits may be expected to go over to the State nonmember banks, and this is no time for wholesale shifting of deposits; besides, the rate of interest on deposits is largely an administrative matter and not one to be incorporated into law.

The amendment to section 24 of the Federal reserve act in reference to real-estate loans and controlling the amount of investment in the banking premises, of course, has its merit for the future, but there are member banks at this time which would be very much embarrassed by this amendment, owing to the amount invested in their banking premises, and the effect would be very disastrous, as there is a very thin market everywhere in the country now for real estate of any size.

The amendment to national bank act, section 5138, requiring national banks to place their shares on \$100 par value within the period of two years is uncalled for now. While I believe the practice of splitting the par value of shares up for the purpose of advancing prices is wrong, yet the damage has been done in this respect, and the amendment should only prohibit reducing the par value of shares below \$100 in the future. There are many national banks having shares of a par value of \$10, \$20, \$30, and \$40 which have been outstanding for over 50 years, and it would be very disturbing to the stockholders of these banks to make an adjustment, and many would be forced to sell their small holdings.

The amendment to section 13 of the Federal reserve act discriminating against 15-day loans of member banks will be a great hardship on member banks for quick short-time loans for daily settlements, and it will also handicap the banks in participating in future Government issues.

The amendment to section 19 of the Federal reserve act altering the rate of reserves against deposits certainly is one which deserves more study, and the regulation affecting the transfer of credits with reserve banks may serve a purpose at certain times and in certain localities, but ordinarily to handicap a bank in the free use of its excess funds at the reserve banks will unquestionably disrupt long-established practice between banks in settling their debits and the accommodation to their customers.

The amendment to national bank act, section 5255, in reference to branch banking does not go far enough. If it is desirable that national banks can have state-wide branch banking in one State, it applies to all States, and if there ever was a need for branch banking it is now, which should be developed under Federal laws and not under State laws. This is the one item in the whole bill that is in the nature of constructive legislation but falls short of nation-wide benefit.

All of the above points will go a long way to discourage membership in the Federal reserve system, and all those requirements in respect to loans secured by stocks and bonds will have a serious effect, as stated above, on the market

value of the securities. (The mere consideration of this bill has, no doubt, had an effect on the market.) The enactment of the regulations in this bill would cause such a disturbance in the banking relations at this time, when everything is at a high tension, that the effect would be very unfortunate.

The inclosed resolution shows you how the Baltimore bankers regard the enactment of this bill at this time, and I trust that you will use your utmost efforts to prevent its passage.

Very truly yours,

CHARLES E. RIEMAN, *President.*

BALTIMORE, Md., *March 22, 1932.*

At a meeting held this date of all members of Federal reserve system in Baltimore it was resolved that it was the unanimous opinion that the enactment of the proposed Glass bill is most inadvisable and highly undesirable at this time.

CHARLES E. RIEMAN,
*President Baltimore Clearing House,
Acting Chairman.*

Banks present: National Central Bank, National Marine Bank, First National Bank, Western National Bank, Balto-Commercial Bank, Baltimore Trust Co., Maryland Trust Co.

Also a letter from Mr. Waldo Newcomer, of Baltimore [reading]:

MARCH 21, 1932.

HON. P. L. GOLSBOROUGH,
United States Senate, Washington, D. C.

DEAR SENATOR GOLSBOROUGH: I thank you for the copy of the revised Glass bill, which I have read and think it is an improvement over the original.

I would, however, like to call your attention to a few details, which may be all right in the bill, but I think should be checked.

Page 7, lines 24 and 25: Should the words "or affiliate" be added?

Page 9, line 1: Should the words "or affiliate" be added?

Page 31, line 3, section (f): What effect will this have on the practice in Baltimore where banks who are members both of the clearing house and of the Federal reserve clear for nonmembers of the clearing house and for clearing house members who are not members of the Federal reserve system?

Page 32, lines 16 to 20: It looks to me like this provision was extremely wide. It would allow a Baltimore bank to make loans on real estate in South Carolina. Was this intended?

Very truly yours,

WALDO NEWCOMER.

The CHAIRMAN. Our first witness this morning will be Mr. James Francis Burke, general counsel of the Pittsburgh Clearing House Association and a former member of the House Committee on Banking and Currency.

STATEMENT OF JAMES FRANCIS BURKE, GENERAL COUNSEL OF THE PITTSBURGH CLEARING HOUSE ASSOCIATION, PITTSBURGH, PA., AND A FORMER MEMBER OF THE COMMITTEE ON BANKING AND CURRENCY OF THE HOUSE OF REPRESENTATIVES

Mr. BURKE. Mr. Chairman and gentlemen of the committee, I wish first to present the formal resolution adopted by the Pittsburgh Clearing House Association on Monday, March 28, 1932, and ask that it be made a part of the record [reading]:

Resolved, That we convey to the Banking and Currency Committee of the United States Senate and to the Members of the Senate and House of Representatives our earnest protest against the approval and enactment of Senate bill 4115, known as the Glass banking bill, upon which hearings are now being held by said committee.

For the following and many other reasons we regard its enactment at any time, and particularly at this time, as unwise and unnecessary:

First. The present agitation or enactment of legislation based upon the theory that our banking system is so defective in structure or so weak in resources as to justify the radical changes proposed in this bill, is certain to create apprehension at a time when assurance and encouragement are most needed.

Second. The dissemination of any such disturbing theory during the present period of earnest effort upon the part of the Government and the business world to reestablish stability and confidence can not fail to nullify to a large extent the beneficial results of recent legislation brought about by the commendable cooperation of the executive and legislative branches of the Government and both political parties in the Congress and its prompt acceptance and approval by the banking and business world generally.

Third. One of the fundamental purposes of the Federal reserve system being to decentralize authority and impose regional responsibilities upon those whose duty it is prudently to administer the banking business throughout the country, we believe it unwise to deprive the directors in the various Federal reserve districts of discretion and responsibility to the extent that this bill would do so.

Fourth. We are convinced also that the unprecedented centralization of authority in the Federal Reserve Board at Washington is certain to weaken, rather than strengthen, the banking structure, in addition to being in direct conflict with the constantly increasing opposition of the American people to the further absorption of local powers and the assumption of purely local responsibilities by the Federal Government.

Fifth. We believe that the curtailment of the present privileges of banks to use their funds in connection with transactions in securities is not only in conflict with normal and well-established methods of sound banking but will inevitably affect the marketability and value of Government securities and ultimately compel banks, in order to subsist, to resort to higher rates of interest on loans and lower rates of interest on deposits, and thus adversely affect business generally.

Sixth. We believe that the restrictions made possible under the provisions of this bill, in the matter of ownership of securities by member banks, regardless of the time limit within which divestment must be made, creates such apprehension and uncertainty as inevitably to compel the sale of large volumes of securities at a time when further enforced deflation would seriously retard business recovery.

Seventh. The result of increasing the reserves of member banks beyond their normally safe requirements, while adding nothing to the soundness of member banks, can not fail to be detrimental to business generally.

Eighth. To abruptly enforce complete separation of affiliates by member banks would result in widespread liquidation of securities at a time when the market is not prepared to absorb them. This, in turn, would impose unnecessary losses upon holders of securities throughout the country.

Ninth. Furthermore, to enact a law which would create uncertainty as to when such separation might be required would have a tendency to undermine confidence among member banks and inevitably induce them to divest themselves of securities lest they be suddenly called upon to do so at a more inopportune time.

Tenth. The limitation of the right of national banks to own real estate or make real-estate loans, would not only bar many member banks from making many legitimate and safe loans on real-estate securities, but where banks are undercapitalized or carry a small volume of time deposits, it would compel calling in the loans now outstanding, and in some cases actually require banks to sell their bank premises and acquire or rent others. This would work hardship upon stockholders and borrowers alike and induce further disastrous deflation of real-estate and security values generally.

Resolved, That a copy of these resolutions be presented to the Banking and Currency Committee without delay.

Mr. BURKE. Inasmuch as this resolution practically traverses the points that have been made here by various witnesses who have preceded me I will not trespass upon the time of the committee for any extended statement, but for a moment I should like to say a word on two phases of this proposed legislation:

First, on the question of the necessity for any such legislation; and
Second, on the question of its timeliness.

I have a very deep-seated interest in the Federal reserve system. I have just as deep-seated an interest in the reputation and distinguished record of Senator Glass, with whom I had the pleasure to serve for many years on the Banking and Currency Committee of the House of Representatives and during the time when we were framing the Federal reserve law; likewise with Senator Bulkley, of Ohio.

Senator GLASS. And incidentally you opposed it.

Mr. BURKE. I did not incidentally oppose it. I opposed it as a main fact. I did oppose the original Federal reserve bill that was sent to us as members of the Banking and Currency Committee of the House and upon which we held on hearings in the committee.

Senator GLASS. Oh, we held hearings for three months.

Mr. BURKE. Yes; of course, subsequently we did hold hearings. But I opposed it at that time because there were vital features of the bill which I regarded as not constructive, not helpful to the banking interests or the business interests of the country.

Senator GLASS. And which were written into the bill and were never changed.

Mr. BURKE. Senator Glass, it is very true that there were many features of the original bill which were retained. At the same time there were many features of the original bill that were stricken out, and I will say that that bill was seriously modified as a result of hearings held in this very room.

Senator GLASS. There were not many changes made. There were some dotting of i's and crossing of t's, but not a fundamental provision of the bill was changed.

Mr. BURKE. Well, of course that is a matter of opinion, and you are entitled to your opinion, and I have great respect for it.

Senator GLASS. No; that is a fact. It is not a matter of opinion, but a matter of record.

Mr. BURKE. Be that as it may, the Federal reserve system has been in vogue now for a period of 19 years.

Now, as to the question of necessity. To my mind it has grown to be the most efficient banking structure in the world. At the issuance of the last statement it had \$5,342,000,000 of reserves. And now taking your statement alone, Senator Glass, that it was given very mature consideration by the Senate and the House at the time of its original enactment, let me say that the bill subsequently was rewritten in certain measures in 1916, when the 15-day rule was written into it, and it was subsequently amended—

Senator GLASS (interposing). You do not mean that it was rewritten but that it was amended.

Mr. BURKE. Well, let us call it that; and it was amended in 1917, when additional changes were made, with the result that the Federal reserve act of to-day is not the outgrowth of the single impulse and the limited thought that was given to the original measure, but is the result of the experience of years, and of the devoted study of gentlemen like yourself.

Now, in addition to that, I will say that the Federal reserve system has justified its existence. It has been a matter of open boast before the public of this country by your friends, Senator Glass, that it piloted us through the World War, that it rendered

the greatest service to the people of this country and to the people of the world that any banking structure of any nation had done.

Now, that being the case it seems to me that after 19 years of a record of that kind, it is a very serious question whether or not it is necessary to modify in any material feature an act of that character and with that record at a time like this.

Senator BROOKHART. Mr. Burke, on that question about its high efficiency let me ask you, or rather I will state first, that it has got into the hands of stock gamblers, and did it have anything to do with the deflation of 1920 and the subsequent inflation, and then the deflation of 1929?

Mr. BURKE. Not any more, Senator Brookhart, than any other unit in our economic structure.

Senator BROOKHART. If it was so tremendously efficient why shouldn't the Federal Reserve Board have laid its hand on that situation and stopped it?

Mr. BURKE. It was efficient in a great emergency. Its business, however, was not to control your impulse or mine. The American people would never have tolerated any banking system that placed in the hands of any set of men the power to say how they should invest their money, or, if you will, squander their money.

Senator BROOKHART. But their business was to keep it out of the hands of speculators and gamblers.

Mr. BURKE. I must most respectfully differ with you about that, Senator Brookhart. The purpose of the Federal reserve structure was to as far as possible decentralize the banking authority, to place upon the bankers of this country regional responsibility in order that they might apply in the administration of that structure the wisdom that had come to them as the result of years of experience.

Senator BROOKHART. There is another point that occurs to me in the matter of efficiency. How about the inflation that went on preceding and during 1928 and 1929, and the deflation that has followed and seems to be continuing? Did it permit that? And is that what you call its efficiency?

Mr. BURKE. My answer to that observation and question is this: There was not a single unit in our whole economic structure, there was not a single class of people in this country, that did not contribute to the inflation of 1928 and 1929. And no one knows that better than you do, Senator Brookhart, because it ran through the agricultural regions of the country.

Senator BROOKHART. Oh, yes; but was the administration of the Federal reserve act efficient in helping that along?

Mr. BURKE. No. But I do want to say that—

Senator BROOKHART (interposing). Well, I want to find out if I can what you think about the character of its efficiency.

Mr. BURKE. Oh, I would not say affirmatively it did that. But I do want to say that the people who had investments in the banks of the country had the right to withdraw them and invest them as they saw fit. That was not the difficulty. If the Federal reserve banks had prohibited people to withdraw their money and use it as they saw fit long before 1928 the people would have lost confidence in the system. They wanted their money available for whatever purpose they saw fit to use it.

Senator BROOKHART. The system was not very efficient in stopping deflation in late 1920 and in 1921, nor in permitting the inflation of 1928 and 1929. Did it have anything to do with the failure of some 8,000 banks as a result of that inflation and deflation?

Mr. BURKE. If you mean by that question to intimate that it had an affirmative influence in bringing that situation about I would answer no. To apply any such reasoning to the situation would be an indictment of the bankers of this country, the directors of the various Federal reserve districts and in turn the Federal Reserve Board.

Senator BROOKHART. Well, I would not hesitate to bring such an indictment against them.

Senator FLETCHER. But, let me ask you, did the Federal reserve banks do what they might have done to check the inflation of 1928 and 1929?

Mr. BURKE. That is a matter of serious discussion and always will be. It was a question of applying the wisdom in the minds of the people at that time. Some thought this was a wise policy and some thought the other was a wise policy. That will always be the subject of debate. And yet I do not gainsay the fact that Senator Brookhart has suggested, as to what happened, and yet I say—

Senator BROOKHART (interposing). Mr. Burke, have you ever studied the cooperative banking system of Great Britain?

Mr. BURKE. Not very minutely.

Senator BROOKHART. Have you ever compared its efficiency with the ups and downs that we have had in the United States?

Mr. BURKE. No; I have not. In fact, I have been too busy since the panic came on to study any foreign banking system.

Senator BROOKHART. Then you are not in a position to say that this banking system we have in the United States is the most efficient in the world.

Mr. BURKE. I do not know of any banking system in the world that has stood the test better. We are one country that is still on a gold basis and we are going along and meeting situations as they arise, and if that does not spell the success and efficiency of the system I do not know what would.

Senator BROOKHART. We first had the greatest production of any country in the world, and then the people suffered the greatest losses of any country in the world, and we have had more bankruptcies than almost any country in the world.

Mr. BURKE. That may be, but what has the Federal reserve system to do with it? The situation that developed was of foreign origin. The panic did not start in this country.

Senator BROOKHART. I think it is directly chargeable to the inflation that was permitted prior to 1928 and the deflation that followed.

Mr. BURKE. Well, Senator Brookhart, you are entitled to your belief. That is a question of opinion on which people differ.

Senator BROOKHART. I object to a system that is so administered that permits both inflation and deflation in that way.

Mr. BURKE. We could discuss that subject interminably and still have an honest difference of opinion. And I will say, Senator Brookhart, that I have very great respect for your opinion.

Now, there is another phase of this subject that I should like to address myself to. There is no question about the fact that in the minds of the people of this country there is the feeling that we need at this moment a liberalization of credit; a banishment of the fear and apprehension that exists in the minds of all classes of people and has existed for the past year.

And in proof of that I will say that the very gentleman who fathered the Federal reserve system, whose name stands out in banking legislation in this country, Senator Glass, rendered a great service to the people of this country in his teamwork with the Chief Executive of this country and other members of both parties in Congress, when he sponsored the Glass-Steagall bill for the purpose of liberalizing credit and giving the people a chance to breathe. And yet in the face of that—

Senator BROOKHART (interposing). On that proposition I wish to remind you that when Senator Glass presented this bill to Congress he stated that one of its great purposes was to stop the use of surplus credit of the country in speculation over in New York.

Mr. BURKE. I understand that, but—

Senator BROOKHART (continuing). And he has adhered consistently to that proposition in all his record, and yet there has been no man who has criticized the administration of this law more than he has because that principle has been violated all along.

Mr. BURKE. That may be. I am not discussing that. But the Senator has confessed to the American people that what we need at this time is a liberalization of credit. And just when we were beginning to stand erect and breathe a little bit of freedom this bill is introduced which, to my mind, would undo in large degree the good that was done as a result of the Glass-Steagall bill and the creation of the Reconstruction Finance Corporation.

Senator GLASS. And it does not interfere with a sentence of it.

Mr. BURKE. You may not think so, but—

Senator GLASS (interposing). Well, I don't think so, and I am quite sure of it.

Mr. BURKE. I am speaking now of the state of the public mind. And while on that point I wish to add: On yesterday a very remarkable statement was made, one of the most dramatic statements ever made in the House of Representatives, made by Speaker Garner. This is what he said:

As sure as I stand in the well of this house I believe with all my soul that if the Congress to-day should decline to levy a tax bill there would not be a bank in existence in the United States in 60 days, that could meet its depositors.

What did he mean by that? That as a result of a single vote on a single section of the tax bill last week there was practically a panic in the minds of the people of this country, and the dollar descended in value in every market of the world. What John N. Garner meant there was, that regardless of the merits or demerits of the tax-raising measure the refusal of the House of Representatives to act promptly on a great economic measure at this time was going to carry terror to the banking and business interests of the country and do untold damage.

Senator BROOKHART. In spite of all this efficiency you have been talking about we have had to create the Reconstruction Finance Cor-

poration with \$2,000,000,000 taken from the Treasury, and have had to have a tax bill that would levy more taxes upon the common people of the country, in order to save us from the worst disaster that ever came along.

Mr. BURKE. Exactly. And in addition to that you failed to mention the National Credit Corporation that went to the rescue of 1,100 banks, and to the defense of—

Senator BROOKHART (interposing). Oh, yes; that is the one that started out and threw up its hands.

Mr. BURKE. Even so that does not prove that any other banking system would have left a better condition in this country.

Senator BROOKHART. I think my suggested cooperative banking system would have left the conditions in the country better and not worse.

Senator GLASS. I want to go on record again as saying that I do not know of anything that happened anywhere in this country that has contributed more to intensify the fear of the people than the largest part of the testimony that has been given around this table by the witnesses who have appeared before us.

Mr. BURKE. In answer to that may I ask you this question in turn: This is banking legislation and who is demanding it? Since these hearings opened you have had before you bankers from all sections of the country, and every one of them has appeared in unanimous protest against this bill.

Senator GLASS. Yes; and they were brought here in an organized protest, just as I think you were.

Mr. BURKE. Suppose they were, yet the fact remains—

Senator GLASS (interposing). Oh! Didn't we have the same sort of protest, and didn't we have resolutions akin to the one you have brought here from the Pittsburgh people, when we passed the Federal reserve act?

Mr. BURKE. Exactly. And isn't it a fact—

Senator GLASS (interposing). Undoubtedly we did.

Mr. BURKE. Exactly, with reference to the original Federal reserve bill.

Senator GLASS. That shows just how much importance is to be attached to similar propaganda.

Mr. BURKE. And right there I will say, Senator Glass, that I think you do yourself an injustice, and I am sure that you do bankers an injustice. The doctrine never has obtained in this country and I hope never will when bankers and business men may not have the right to come here and petition Congress and make known their views as to legislation.

Senator GLASS. Nobody questions that.

Mr. BURKE. And you can not impeach them on the theory that they are dragged here. I say they are coming here voluntarily because they are the men who have the confidence of their communities, and they are the people who have conserved the resources of this country.

Senator GLASS. We are not simply guessing but we know why they were brought here, and we have suggested it to them after they got here.

Mr. BURKE. Do you find fault with their coming here? Do you deny their right to come here and present their views?

Senator GLASS. No.

Mr. BURKE. Then there can be no complaint of their coming.

Senator GLASS. I do not admit that you have the right to question my opinion as to why they were brought here, nor what was done after they got here.

Mr. BURKE. Certainly not. But you made the statement, and while I am not questioning at all your right to make it, I am trying to answer it.

The CHAIRMAN. Let the witness proceed.

Senator BARKLEY. Mr. Burke, do you condemn this whole bill or do you admit that there are any features of it that are constructive?

Mr. BURKE. There are features of it that have been repeatedly approved by gentlemen who have been before you, or at least they have said that they have merit. But after all, to my mind the question at this time is, whether or not a measure that has survived for 19 years and rendered good service is in such a precarious condition, is such a weak structure, so weak either in structure or resources, that it calls for a drastic modification at a time when the public mind is in its present state.

Senator BARKLEY. Why is it in that state? We have been sitting here for two and a half years watching bank after bank go to the wall and Congress has done nothing about it, no legislation that has been passed as yet has done anything about it fundamentally; perhaps there has been a temporary remedy to keep the patient alive until nature can take its course, but shall we sit here and do nothing when the people are demanding something that will give the banking system strength and influence?

Mr. BURKE. Senator Barkley, if your premise were correct your theory would be that you can correct the present condition by legislation. I do not believe you can. I do not think you can refill the empty tills of the banks of this country by mere legislative fiat.

Senator BARKLEY. No; but we owe the duty to the public to keep any more from failing.

Mr. BURKE. And you owe a duty to the public to do nothing that will cause further deflation and greater destruction.

Senator BARKLEY. I agree with that but I am somewhat like the old colored preacher who was dismissed from his pastorate because he could not tell the people wherein; he could not tell the people wherein although he could "argify and sputify" on every subject. Now, Mr. Burke, wherein will we injure the people by enacting this bill into law?

Mr. BURKE. May I bring home this thought to you?

Senator BARKLEY. And I am intensely in earnest about it.

Mr. BURKE. No doubt you are.

Senator BARKLEY. I am not committed to any single provision of this bill, but I do want to know, in view of the duty of Congress and the people's suspicion in this whole situation that has been brought about by somebody and I am not charging anybody with it, but we certainly ought not to permit if we can help it a condition to be perpetuated in this country that will make it possible for any disaster like this to overcome the country. The question is whether we are going to try to remedy it while we are sick and know what

the trouble is, if we do, or wait until we get well, and then maybe the doctors will decide that we can not afford to do it while we are well because it might make us sick again. That is a homely sort of philosophy but it is one that appeals to me.

Mr. BURKE. It is very sound from your viewpoint. But why in the world would these men who are the trustees of their communities back home under this regional banking system that we established for the deliberate purpose of decentralizing banking authority of this country; I say why would they come here from all parts of the country and say to you that this legislation would damage the banking structure, and that it would be inimical to the general interests of the American people? Can you gainsay for a moment their interest?

Senator BARKLEY. No; and I do not. I do not impeach their interest, their integrity, their good purpose, or their right to come here. And as far as I am concerned I have welcomed their testimony in the sense that I want light on this subject.

Mr. BURKE. All right.

Senator BARKLEY. But after all it seems to me a mistake to take the position that Congress does not owe some duty even in a crisis to try to protect the people against a recurrence of it if we can do it. Maybe this bill does not do it, but if it does not I should like for somebody to offer a constructive measure that will.

Mr. BURKE. We agree with you on that.

Senator BARKLEY. We have all floundered around for lack of leadership, and it has been just as true of banking matters as of politics.

Mr. BURKE. I fully agree with you, Senator Barkley, that Congress should do all in its power to lead the American people out of this dilemma. There is no difference of opinion about that. What I am questioning is, the wisdom and necessity of enacting this particular measure at this time.

Now let us look at the situation from a practical legislative standpoint. You have a congested calendar both in the Senate and the House. You are going to have an interminable debate on the tax bill. You are going to have great difficulty concluding this session of Congress by June 10 if you gentlemen should decide to adjourn about that time for the national conventions; you will have great difficulty in passing even the appropriation bills and other outstanding measures without any regard whatsoever to this measure.

And what will be the result if you press this measure? You will inject into the arena of debate a measure that has given rise to very serious differences of opinion up to this precious moment, and that will continue for the next six or nine months. The people want to breathe freely, the people want to be out of an atmosphere of apprehension as it were, to go about their business. These bankers here to-day ought to be back home attending to their business, trying to revive and restore confidence in their communities.

Senator GLASS. I agree with you on that thoroughly.

Mr. BURKE. But as a result of your measure, Senator Glass, it is necessary for them to be here in an effort to protect their own interests and those of their communities.

Senator GLASS. Point out to us any provisions of this bill that would do all these disastrous things you talk about. You don't need to talk to us about legislative strategy or procedure. We as

Members of Congress know those things quite as well and perhaps a little better than you do.

Mr. BURKE. Nobody has denied that, but I have attempted to point out the situation as I see it.

Senator GLASS. Just address yourself to the provisions of the pending bill.

Senator FLETCHER. You have alluded to drastic provisions of this bill. What are those provisions and what are your objections to them?

Mr. BURKE. The Comptroller of the Currency and the governor of the Federal Reserve Board on yesterday pointed out in detail where they differed with you on the measure.

Senator GLASS. Didn't you hear the Comptroller of the Currency say that he thought legislation at the present time was imperative?

Mr. BURKE. No; not imperative.

Senator GLASS. You did not hear him say that?

Mr. BURKE. No; not that it was imperative.

Senator GLASS. But he did.

Mr. BURKE. I beg your pardon.

Senator GLASS. He did say that, and the governor of the Federal Reserve Board said he thought it very desirable, and that that was the reason he made these recommendations.

Mr. BURKE. But I am talking about this bill. Before he made that statement he spent an hour and a half dissecting the bill and pointing out its evils.

Senator GLASS. As a matter of fact he didn't do anything of the kind. But if you will simply take the proposals he made and tell me the difference between his proposals and the provisions of this bill you will do a service to this committee.

Mr. BURKE. You understand that—

Senator GLASS (interposing). Just point them out.

Mr. BURKE. Senator Glass, you, of course, understand the English language and—

Senator GLASS (interposing). I certainly do.

Mr. BURKE. Well, I will say—

Senator GLASS (interposing). Just point out to us the difference between the proposals of the Federal Reserve Board and the provisions of this bill.

Mr. BURKE. You said on yesterday—

Senator GLASS (interposing). Oh, let us come down to concrete things. Take a section of the bill and tell me the difference between the proposal of the Federal Reserve Board and that section.

Mr. BURKE. Well, I will say—

Senator GLASS (interposing). Just take up the bill and pick out any section of it and tell me wherein there is a difference between the proposal of the Federal Reserve Board and that section of the bill.

Mr. BURKE. Do you want me to go into an analysis of the bill?

Senator GLASS. Yes.

Mr. BURKE. If you want me to take up the bill section by section I can do it.

Senator GLASS. All right, and tell me the difference.

Mr. BURKE. I can do it at great length, but keep this in mind, that the last thing you said on yesterday to Governor Meyer was—

Senator GLASS (interposing). Just point out to us the difference. Mr. BURKE. You said to Governor Meyer that you did not agree with his theories or his amendments.

Senator GLASS. You just go ahead now and point out to us the differences between the proposals of the Federal Reserve Board and the provisions of this bill as you claim. As a matter of fact I agree with a good many of those suggestions.

Mr. BURKE. I understand, but on yesterday you made the blanket statement that you disagreed with them as a general proposition.

Senator GLASS. No; I did not make any blanket statement.

Mr. BURKE. Then if you and Governor Meyer are in accord it is all right.

Senator GLASS. But you and Governor Meyer are not in accord. He says this should be done and you say not.

Mr. BURKE. No. What I say is—

Senator GLASS (interposing). The Comptroller of the Currency said legislation was extremely desirable.

Mr. BURKE. But this is what Governor Meyer said—

Senator GLASS (interposing). Let us not get off on that. Let us stick to the matter of comparison.

Mr. BURKE. He said legislation such as he suggested here would be timely at this time.

Senator GLASS. Take section 3 of the bill and let me know the difference between the proposal of the Federal Reserve Board and what is contained in that provision of the bill.

Mr. BURKE. Senator Glass, I have page after page here on all sections of the bill.

Senator BARKLEY. Mr. Burke, what is that document the pages of which you are turning over?

Mr. BURKE. This is an analysis made in Pittsburgh by our clearing house association.

Senator GLASS. I am not talking about the Pittsburgh Clearing House Association but the suggestion of the Federal Reserve Board.

Mr. BURKE. Very well.

Senator GLASS. Tell me the difference.

Mr. BURKE. I was going to tell you—

Senator GLASS (interposing). The Pittsburgh Clearing House Association could not have passed on that recommendation made by the Federal Reserve Board because it was only made on yesterday.

Mr. BURKE. Oh, no; but I am not talking about that at all.

Senator GLASS. Go ahead and tell me the differences.

Mr. BURKE. You were asking about section 3 of the bill.

Senator GLASS. All right. Go ahead.

Mr. BURKE. And you were speaking about you and the governor of the Federal Reserve Board being in accord. When you said the governor stated it was advisable to enact this legislation, and when you stated that Comptroller Pole said that the passage of this legislation was imperative, I am quite certain, Senator Glass, that your memory was at fault.

Senator GLASS. Oh, no. But you are here saying nothing should be done at all.

Mr. BURKE. No; I did not say that.

Senator GLASS. Well, let the shorthand reporter read his notes of what you said.

Mr. BURKE. No; I did not say that.

Senator GLASS. Let us have the shorthand reporter read his notes of what you said and see if you did not say that.

Mr. BURKE. What I said was this: That legislation of this nature at this time was untimely. And I said I believed the Federal reserve structure was so inherently strong, and for the reasons that I pointed out, it was not necessary to inject amendments at this time and bring about a discussion of this delicate matter during present economic conditions. That is what I said.

Senator GLASS. Well, the record will show.

Mr. BURKE. All right. But, of course, Senator Glass, I have a high regard for your opinion.

Senator BARKLEY. Mr. Burke, let me ask you this: Our banking history in the last two and a half years has been very unfavorable when compared to the banking history of other countries. Whatever may be the differences we might not find it profitable to go into them now. But we have had a deplorable accumulation of bank failures and there is more or less lack of confidence on the part of the people in our banking system. What is your remedy for that?

Mr. BURKE. Senator Barkley, the remedy for that is the chaisement and wisdom that comes from experience. You can not legislate it into the minds of bankers. The bankers of this country have had their lesson; and as a result of what transpired in 1927, 1928, and 1929 the bankers of this country have learned a great lesson.

Senator BARKLEY. But are they going to profit by it?

Mr. BURKE. Yes; and they will profit by it without legislation.

Senator BARKLEY. How do you know?

Mr. BURKE. It is the history of the human race.

Senator BARKLEY. Not always.

Mr. BURKE. It is their history.

Senator BARKLEY. Your idea is that we ought not to do anything as a result of the experience we have had in the last two years and a half, and that if there are weak places in our banking system they ought not to be strengthened at this time.

Mr. BURKE. Well, I think it is unnecessary at this time. I think the system as a central structure should be allowed to exist without any repairs at the present time. I think the country will be better off if this bill were eliminated from the field of discussion for the time being.

Senator BARKLEY. Do I understand that your attitude is purely as a representative of the Pittsburgh Clearing House Association and not as general attorney for the Republican National Committee?

Mr. BURKE. The Republican National Committee has nothing to do with me in this matter. It is my own personal view. I should like to be in accord with you, Senator Barkley, and I hope when you sound the keynote in the Democratic National Convention you and I will be in perfect accord.

Senator BARKLEY. Well, I will be willing to receive suggestions from you.

Senator BARKLEY. Then am I to understand that these are your personal views and that you are not representing the Pittsburgh Clearing House Association?

Mr. BURKE. These views I am expressing now I would say are my own personal views as an individual, as a national bank director,

and as one who has had somewhat to do with legislation of this character. My associations with you, Senator, have been very pleasant and profitable.

Senator BULKLEY: As to that resolution from the Pittsburgh Clearing House Association, was that in line with what you have been saying?

Mr. BURKE. As to the general objections to the bill; yes,

Senator BULKLEY. Does it generally take the position that the Federal reserve law is now so good it ought not to be tampered with?

Mr. BURKE. It takes the view that it is sufficiently strong to survive the present emergency, and that it would be wiser not to tamper with it at this time.

Senator BULKLEY. Do you contend that there is anything in this Glass bill that is in any way a modification of the intent of the original Federal reserve act?

Mr. BURKE. That is a matter, Senator, of debate. It is in the state of mind, whether it is a fact or not. I am dealing with the thing that Speaker Garner dealt with yesterday on the floor of the House. You can not escape it.

Senator BULKLEY. You can not put this in any such class as to say that it is equivalent to failing to balance the Budget. That would just make you ridiculous. You do not say that, do you?

Mr. BURKE. No; I do not say that is ridiculous.

Senator BULKLEY. Of course you do not.

Mr. BURKE. No; but—

Senator BULKLEY (interposing). Let us forget about it.

Mr. BURKE. But it bears the general relation to the same subject, Senator. It has to do with the creation and the promulgation of uneasiness. That is what it has to do.

Senator BULKLEY. Yes; you have said that, but I want to go one step further now and I want you to show me how a measure that is designed to carry out the purpose and intent of the Federal reserve act, which you so highly praised, is going to create so much uneasiness. If you do not agree that it does carry out the purpose and intent of the Federal reserve act, show me wherein there is a difference in principle.

Mr. BURKE. Well, your curtailment—you curtailed credits. There is no question about that. You modified the matter of administration. You centralized authority. There is no feeling in this country growing stronger day by day.

Senator BULKLEY. You are not telling us anything that is a departure from the principles of the Federal reserve act. If you say the act is so good, why shouldn't its principles be enforced and tightened up?

Mr. BURKE. Senator, you have increased the powers of the Federal Reserve Board as compared with those that existed previously.

Senator BULKLEY. In some respects we increased them and in some respects we did not increase them, but diminished them. Some of the principal criticism is that we diminished the power of the Federal Reserve Board in some respects.

Mr. BURKE. My criticism would be that your enhancement of the powers of the Federal Reserve Board is detrimental to the country.

Senator BULKLEY. You would not criticize that 1 per cent penalty rate, then?

Mr. BURKE. I do not see any necessity for it.

Senator BULKLEY. That is a restriction on the powers of the Federal Reserve Board.

Mr. BURKE. That may all be, but at the same time, it is an imposition and an additional burden on the borrowing banks.

Senator BULKLEY. I would like to have you get back and answer the question as to wherein we depart from the principles of the Federal reserve act.

Mr. BURKE. The word "principles" is a very broad proposition. You might state a detail here and there and say it is still within the general principles.

Senator BULKLEY. Yes; but you say there are very drastic changes. What are they?

Mr. BURKE. Well, the power you give to the Federal Reserve Board themselves to determine the percentages within which investments can be made by banks in various regions. You are taking away from the various regional directors the power that was lodged in them as a result of the protest at the time the Federal reserve act was passed against a central bank. That was repugnant to you, to your associates, and to other people in the country. For that reason you divested them of these powers and distributed them through the various sections of the country. Your tendency now is, according to my impression, to deprive the local authorities of their powers and vest them in the Federal Reserve Board.

Senator BULKLEY. Tell me how much that is done. What are the several things that we take away from a local bank?

Mr. BURKE. That one thing, for instance.

Senator BULKLEY. That is one.

Mr. BURKE. That is an illustration.

Senator BULKLEY. What else is there altogether?

Mr. BURKE. Now, I could go through that, Senator, at some length; but, as I say, that is an illustration of it, and your open market—

Senator BULKLEY (interposing). Your implication is, of course, that they run all the way through the bill, and yet you can not name another instance of it.

Mr. BURKE. Oh, yes. Yes, there are other instances.

Senator BULKLEY. Well, I said you could not name them.

Mr. BURKE. How many sections are there in the bill? There are 21 sections, and every one of them is a modification.

Senator BULKLEY. Of the principles of the Federal reserve act?

Mr. BURKE. Well, no; they are a modification of the Federal reserve act. You might call it a principle. You may say that they are alterations of the act, but not alterations of the principles; and other people believe that it is an alteration, and the bankers of the country think that.

Senator BULKLEY. They are alterations to enforce the law as originally intended.

Mr. BURKE. There is no necessity for reenforcing it as enacted. It was enacted and enforced for 19 years, and enforced successfully and admirably.

Senator BULKLEY. There has been plenty of necessity; more than the world ever saw.

Mr. BURKE. That may be true. It is a matter of opinion.

Senator WAGNER. Mr. Burke, if we were not in a disturbed economic state, as you say, would you still oppose the major provisions of this bill?

Mr. BURKE. From my standpoint I do not know that I would. I am not sure about that. But because I am dealing solely from my viewpoint with the timeliness of this matter, it might be; I might modify my views about the intensity of the evil that would follow this legislation. I might not. I might adhere to it. I do not know, Senator.

Senator WAGNER. You are not determined in your own mind—

Mr. BURKE. No.

Senator WAGNER. As to whether any of these provisions would improve the system?

Mr. BURKE. No. I determine in my own mind that they are unnecessary.

Senator WAGNER. Under any circumstances?

Mr. BURKE. I think you have got a great structure and I think it is a great monument to Senator Glass and Senator Bulkeley and his associates.

Senator GLASS. For the record, in order that it may be determined who is accurate and who is not, the witness does not think there should be any legislation at this time, and suggested that neither the Federal Reserve Board nor the Comptroller of the Currency thought there should be any legislation at this time; I have here the hearing of yesterday in which I asked the Comptroller of the Currency if he was fearful of legislation at this particular time, and he said:

I think legislation would be a very good thing. I am not saying that there should be any disturbing or drastic legislation, but I do say legislation of that character—

speaking of the most controverted provision of the bill, branch banking—

would be immensely helpful.

And so on.

Governor Meyer, being on the stand, was asked by me if he thought there should be legislation immediately along the line suggested by the Federal Reserve Board.

Mr. MEYER. Yes; I think it should. I am not afraid to say that as amended I would welcome the passage of the bill.

So that the board did not engage in an idle gesture when it sent up to the committee some proposed amendments to this bill, most of which did not disagree in essential and substantive provisions from the bill itself. They really want us to incorporate those amendments to the bill and pass it.

Senator FLETCHER. He further said that he agreed generally in the purpose of the bill; had no objection to the bill itself.

Senator GLASS. Yes; and he proposes—the board unanimously, you understand, something that I venture to believe has not happened since the foundation of the system, agreed that these amendments should be made to the bill, many of which I am sure the committee will accept without dispute or much discussion, others of which are not in disagreement with the substantial purpose of the bill, and not much in disagreement with the text of the bill, and the board wants us to incorporate those amendments in the bill and

pass it at once. So that by that record it may be determined who is accurate and who is inaccurate.

Mr. BURKE. Thank you, Senator.

The CHAIRMAN. The next witness is Mr. Bruce, of Baltimore.

STATEMENT OF HOWARD BRUCE, CHAIRMAN OF THE BOARD OF THE BALTIMORE TRUST CO., BALTIMORE, MD.

The CHAIRMAN. State your full name and address and business connections to the reporter, Mr. Bruce.

Mr. BRUCE. My name is Howard Bruce, Baltimore, Md.; chairman of the board of the Baltimore Trust Co.

Mr. Chairman, I have prepared a statement, and might I be permitted to read that statement first and then try to answer any questions?

The CHAIRMAN. If agreeable to the committee. That requires unanimous consent.

Senator TOWNSEND. That is agreeable to me.

The CHAIRMAN. If you would rather do that, I think we would all agree to it.

Mr. BRUCE. I start with the theory that there is nothing sacrosanct about the Federal reserve system. Like every other system in the process of evolution, it is going to be changed; and unquestionably there are changes that are needed in this system. I approach it more with a definite feeling about the changes that are proposed to be made by this bill at this time and their bearing on what I think is the condition of business and finance in this country.

I feel that at the present time when we are in the depths of the greatest depression which this country has ever experienced, no legislation should be proposed that is even open to the suspicion of retarding our recovery from the present business stagnation, following the violent deflation through which this country has gone during the past two and one-half years.

The formation of a liquidating corporation is clear of any such suspicion. There may be wide differences of opinion as to the source from which its capital should be derived, and as to the machinery set up for its operation; but there is an almost unanimous indorsement of the creation of an agency that will return to the channels of trade the assets now frozen in closed banks.

Affiliates: There is unquestionably the need of normal regulation and control of banking affiliates. However, in the present situation the drastic regulating provisions contained in the bill can not fail to have an unfortunate effect upon existing conditions, even if such effect is to some extent in the form of a feeling of uncertainty and unrest.

Section 9 limits the sum which a parent bank may loan to an affiliate to 10 per cent of the capital and surplus of the parent bank, and such loans must be secured by 120 per cent of listed exchange securities or 100 per cent of either eligible paper or savings banks securities, neither of which would be for the most part in the possession of an affiliate unless it happened to be a banking institution. The enforcement of this provision will mean radical liquidation in the case of many affiliates.

The provision of section 25, page 49, paragraph 2, I interpret as meaning that at the end of a 3-year period the affiliate must be completely divorced from its parent company. This appeals to me as a most drastic provision, as it is certainly possible to regulate and control undesirable activities without abolishing an agency of great importance in the distribution of securities and other necessary functions.

Increase of reserves: Section 13 provides for increasing reserves against time deposits over a 5-year period to a figure equal to the present reserve on demand deposits. The Federal reserve system does not need this fund, as it has been and is now able to meet all demands upon it for credit. The depositors are not further protected, as their protection is measured more by the character of assets of the banks than by the amount of their reserve. The banks' loaning power and earning capacity are both reduced.

The worst of its effects will be borne by the outlying banks in rural communities holding a larger proportion of time deposits than the city banks.

Segregation of assets back of time deposits: Much might be said on the provisions of this section, but the most important consideration, to my mind, is that, even though its action is spread over a period of 2 years, it is bound to bring about a disruption of the credit structure of the country. Many banks, particularly those in rural communities, have a large percentage of their time deposits tied up in loans for the benefit of commerce and agriculture in their surrounding territory. Such banks would be compelled to liquidate a large proportion of these loans and invest the funds so obtained in real estate or specified securities.

Limitation of interest on deposits: Section 24 limits the rate of interest that may be paid on deposits. This seems to place the member bank at a disadvantage in competition with nonmember banks. Money is certainly a commodity, and I see no reason why member banks should not be free to pay the rates necessary to hold their deposits.

Control of collateral loans and security holdings of member banks: The provisions undertaking to control the holding by member banks of securities, either as investments or collateral, run all through this bill.

Section 8 gives authority to six members of the Federal Reserve Board to fix the percentage of capital and surplus of any member bank that may be represented by loans on collateral securities, taking out of the hands of the board of directors one of its principal functions.

Section 3 places the discretion in the hands of the Federal Reserve Board as to what constitutes undue or improper use of credit facilities and gives arbitrary power to the board to suspend a member from use of the credit facilities of the Federal reserve system.

Section 11 establishes an increased rate upon 15-day borrowing and places the power in the Federal Reserve Board to suspend a member bank as a borrower from the Federal reserve bank, if such member bank should increase his outstanding loans on collateral security, despite a warning from the District Reserve Bank or the Federal Reserve Board.

Section 15 restricts the amount of investment securities of any one obligor that may be held by a national bank to 10 per cent of the total amount of the issue outstanding, and further restricts the aggregate amount of securities which may be owned. Both of these provisions will bring about a forced liquidation of national bank holdings and will have a further depressing effect upon the market.

This bill throughout its numerous provisions seems to attempt by edict to outlaw the owning of securities, the trading in securities, and the loaning of money upon securities, and to further assume that the blame for the present situation in this country is due to the loaning of money upon collateral securities.

It seems to me impossible to segregate the speculative loan upon collateral from the normal business loan of this character, or to restrict the credit on collateral and at the same time maintain a freedom of credit on short-time paper or Government securities. The whole structure of business of this country has been built up by the wide distribution of securities. The effort to drastically restrict and to control speculation, it seems to me, will result in evils of vastly greater weight. The funds of savings banks, insurance companies, and, in fact, a great part of the wealth of the country, is invested in securities. Any action aimed at the speculative which restricts the free marketing of securities, and depresses their value, will in one way or another affect every man, woman, and child in this country.

A prerequisite to emergence from the present depression is an atmosphere of public confidence, and not one of uneasiness or uncertainty. As I see it, there is nothing in this bill other than the provision for a liquidating corporation, and a few minor provisions, that will not result in creating an atmosphere of uncertainty and unrest, and consequently, if the bill is enacted into a law, or if the possibility of its enactment hangs over the country for any length of time, a further depression of security values will follow. People buy marketable securities for the income to be derived and for the reason that they believe they are readily marketable and in time of need they can readily borrow money upon them as collateral. A denial of this right, in an effort to reach the speculator, is grossly unjust. What I am interested in primarily, and what every other thinking man in this country is interested in at the present moment, is to aid and assist in the emergence from the frightful condition of depression and unemployment from which we are suffering.

If legislation is necessary or desirable to limit any future riots of speculation, such as culminated in the year 1929, I am sorry to say I believe we have a considerable lapse of time ahead of us before we will meet the next such issue, and I can see no possible justification, in a period such as the present, to hurry through drastic provisions which in my opinion will bring on a further deflation of securities and prolong the period of depression.

Senator FLETCHER. Mr. Bruce, you said it was very important to preserve this free distribution of securities.

Mr. BRUCE. Yes.

Senator FLETCHER. And that adds to the prosperity generally. It is not a fact that, prior to 1931, 1929, and 1930, there was a distribution of about 70,000,000,000 of securities in this country, stocks,

bonds, foreign and domestic, unloaded on the public, and in practically every instance the public losing everything they put in? Do you think that is a good thing to do?

Mr. BRUCE. No; but I do not think at the present time, with the provisions of this bill, that you are going to aid that situation.

Senator FLETCHER. One of the effects you said was to check this distribution of securities.

Mr. BRUCE. Well, you limit the owning of securities by an association.

Senator BULKLEY. Mr. Bruce, are you referring there to page 36 when you say we limit that?

Mr. BRUCE. That is the one that limits to 10 per cent the amount of any one issue held by a national bank.

Senator BULKLEY. Yes.

Mr. BRUCE. And further limits the total security.

Senator BULKLEY. That is what it does not do, and I thought you probably misunderstood that. I do not blame you for the misunderstanding.

Mr. BRUCE. It certainly reads that way.

Senator BULKLEY. Yes; I do not blame you for the misunderstanding, but I think your criticism ought to be withdrawn in the light of what is really meant. That has been the custom, those who have misunderstood that and had it explained to them have usually withdrawn the criticism.

Mr. BRUCE. What does it mean?

Senator BULKLEY. It means of any one issue.

Mr. BRUCE. Well, 10 per cent—that would prevent a bank from taking an issue to cover a bad loan.

Senator BULKLEY. Yes; it would prevent taking more than 10 per cent of that issue.

Mr. BRUCE. There are constantly instances where a bank will take a mortgage or something in the form of a security issue to cover a frozen loan.

Senator BULKLEY. Yes; it does that. It does prevent that.

Senator GLASS. Can you loan more than 10 per cent to a merchant?

Mr. BRUCE. This is 10 per cent upon one issue, Senator.

Senator GLASS. I understand that; yes.

Senator BULKLEY. Ten per cent of any one issue.

Mr. BRUCE. Any one issue.

Senator BULKLEY. That is right.

Mr. BRUCE. Banks frequently in the normal course of lines of credit get into a position where a loan is frozen, and, in an effort to protect a loan, they take a mortgage or some issue of securities as protection.

Senator GLASS. What percentage would you prescribe as a limit? Do you think a bank ought to be allowed to take the whole issue of a corporation?

Mr. BRUCE. I think the general clause that Governor Meyer suggested as a substitute for section 3, section 8, section 11, and section 15, the general clause giving authority to the Federal Reserve Board, covers that. I think they have the authority now in a moral way, if not a legal way, to control.

Senator GLASS. In other words, you would not limit the authority by statute or even suggest it by statute?

Mr. BRUCE. No.

Senator GLASS. But you would give the Federal Reserve Board unlimited authority to deal with a matter of that sort, would you?

Mr. BRUCE. I do not know whether you have got to write it into the law or let the present unwritten power act—the power lies there now. I do not want to go under cross-examination on the English system, because I am not an expert, but my impression is that most of the English system and the working of it is based on custom that has gradually grown up. I think the Federal Reserve Board has the power now.

Senator GLASS. I think so, too, Mr. Bruce, but the board does not exactly think so. There has been a great division of opinion on that question, and the matter has been litigated in the courts.

Mr. BRUCE. I have no objection to that clause suggested by Mr. Meyer.

Senator GLASS. And two decisions have been rendered to the effect that the board has that power. I think undoubtedly it has always had that power, and we intended to give it that power; but around this table there has been a great discussion and a bitter attack upon this bill upon the score that it gives the Federal Reserve Board too much power, and now you say that you want their proposed section 3, and I am not objecting to it. But you must understand that their proposed section 3 confers in this respect unlimited power on the board.

Mr. BRUCE. Yes.

Senator BULKLEY. I take it Mr. Bruce disagrees with Mr. Burke on that subject.

Senator GLASS. He disagrees with many of the others.

Mr. BRUCE. I was busy studying my own notes and I can not say that I followed Mr. Burke's testimony.

Senator WALCOTT. Mr. Bruce, I understand you to say now that you approve of the suggestion made by Governor Meyer before with respect to section 3?

Mr. BRUCE. I think I do. All I could say about Mr. Meyer's suggestion is based upon what I have read in the limited time while I was motoring to Washington from my home this morning.

Senator GLASS. Most of it is contained in this bill, the text.

Mr. BRUCE. No; there is a difference. It does not apply this power only to collateral loans. It spreads it out to all other loans.

Senator GLASS. And to that extent still enlarges the power of the Federal Reserve Board?

Mr. BRUCE. Yes; I think it makes it sounder.

Senator WALCOTT. But you approve of that?

Mr. BRUCE. Yes; I have no objection. But your section 3 treated only collateral loans.

Senator GLASS. No; this extends it to commodity loans.

Mr. BRUCE. All right.

Senator GLASS. The point I make is that you disagree with these various other witnesses when they assailed the bill upon that section or upon the power that it gives to the Federal Reserve Board. You do not agree with that, do you?

Mr. BRUCE. I do not agree with that so far as Governor Meyer's section 3, as I understand it, goes.

Senator GLASS. Yes; I understand.

Senator BULKLEY. Now, Mr. Bruce, I would like to get back here to section 15. You have made a criticism which is perfectly clear cut and which can stand without argument at the moment, that this section would prevent a bank from taking over a whole issue, whether for the purpose of clearing up a bad loan or any other purpose.

Mr. BRUCE. Yes.

Senator BULKLEY. That is true.

Mr. BRUCE. Yes.

Senator BULKLEY. Now, that is an understandable criticism. But you did say in your prepared statement that what follows there would cause an increased liquidation. Of course, that is not so, is it?

Mr. BRUCE. Yes; it is so, because I think many national banks hold at the present time more than 10 per cent of individual issues.

Senator BULKLEY. Yes, but this only provides that they shall not acquire it hereafter.

Mr. BRUCE. Is not the word "holding" in that section?

Senator BULKLEY. Yes. I will not defend the wording of it, Mr. Bruce.

Mr. BRUCE. I am discussing what it says.

Senator BULKLEY. I am not trying to put you in a hole. I am trying to arrive at the truth, and I agree with you that the wording is not appropriate to express the intent. But the intent of it is that the bank shall not hereafter acquire for holding more than these limits of any one security. It is subject to the criticism you made for whatever merit it has, but the other criticism, because of too much liquidation, does not stand, does it?

Mr. BRUCE. Yes; as it is worded it stands. Might I ask one other thing: Is it the intention of that act that they should not hold in any form of security more than 15 per cent of their capital and 25 per cent of their surplus? That is the way it reads to me.

Senator BULKLEY. Of any one security.

Mr. BRUCE. No; no; as I read it. It is involved, and as I see restricts total holdings of all securities.

Senator WAGNER. We have agreed that that should be amended.

Mr. BRUCE. It is involved, and I believe it covers all issues.

Senator BULKLEY. Yes; I agree with you that the wording is unfortunate, but I want you to take our statement of what is the intent of it.

Senator GLASS. We have explained to witness after witness, at least a score of them—well, I won't say at least a score of them, but more than a dozen of them—just what the intent was. We have agreed that the language is involved and needs clarification, and yet each succeeding witness comes back to the same criticism.

Mr. BRUCE. Well, I have tried to study this particular bill, Senator. I have not read any other testimony, and I have tried my best to study this bill, and I have had a difficult job.

The CHAIRMAN. There seems to be no disagreement on that point. Suppose we proceed to something else.

Mr. BRUCE. I think that the section 3 proposed by Governor Meyer gives ample control, and I question the advisability of putting a rigid limit into this bill. I question it.

Senator WAGNER. In other words, Mr. Bruce, even if it applied to only future issues—

Mr. BRUCE (interposing). I question it.

Senator WAGNER. You still oppose the 10 per cent limitation?

Mr. BRUCE. Absolutely, the 10 per cent; and I question that whole thing. I think the criticism of the Federal Reserve Board, if anything, is for not exercising power rather than for not having power.

Senator GLASS. Well, undoubtedly; and what assurance have we, Mr. Bruce, that it is going to exercise it hereafter? Take section 11 of this bill: That is the 15-day period. Existing law there provides that the Federal Reserve Board may have unrestrained power to control the rate of 15-day paper, which is a special privilege, not originally designed and not originally incorporated in the act. Why would you say we gave the board the right, the unrestricted right, to make a rate on that transaction?

Mr. BRUCE. You stipulated that it must be at least 1 per cent higher.

Senator GLASS. I am not talking about that now; I am talking about why we gave that right. That is a limitation upon the board, a restriction upon the board rather than an extension of its power. The 15-day provision of the bill, which has been in there for 16 years, you will admit, gives the board unrestricted power?

Mr. BRUCE. Absolutely.

Senator GLASS. To levy a special rate on these transactions, does it not?

Mr. BRUCE. Yes.

Senator GLASS. It has never been exercised?

Mr. BRUCE. No.

Senator GLASS. Don't you think it might have been exercised in 1928, 1929, and 1930?

Mr. BRUCE. Senator Glass, I was not a banker in that time. I was an observer, and I would not——

Senator GLASS (interposing). Well, I am not a banker at all at any time. I am an observer. Don't you think the board might very well have applied that authority then?

Mr. BRUCE. I think they had powers that might have to advantage been applied in those years that were not applied.

Senator GLASS. Then what assurance have we that hereafter they will be applied?

Mr. BRUCE. Senator, I do not believe you can substitute legislation for discretionary power in as definite a way as that. It seems also to be aimed particularly at the——

Senator GLASS (interposing). Stock gambling?

Mr. BRUCE. Investments in stocks. Haven't you got to have some discretion in somebody? You can not set down and predict conditions that are going to exist for all time.

Senator GLASS. Nobody seems to have exercised the discretion at the imperative moment when it should have been severely exercised, and it was because of that default that the country is in such condition as it is to-day, and what we are trying to do is to avert a repetition of that.

The CHAIRMAN. The Senator from Virginia will recall that we had members of the Federal Reserve Board here before this committee in the spring of 1928.

Senator GLASS. Yes.

The CHAIRMAN. And they did not see the need of any action then.

Senator GLASS. Now, Mr. Bruce, all right, sir; I think you and the committee are in agreement as to the desirability of doing some things. You make the broad statement that a person buys securities for the purpose of collecting the interest on the investment. Would you apply that statement to conditions in 1928 and 1929 on the New York Stock Exchange?

Mr. BRUCE. To a tremendous number, yes; to a tremendous number.

Senator GLASS. You do not agree then with that New York paper which takes pride in saying that it represents the vested interests of the country and which has said that at least 90 per cent of the transactions of the previous week on the stock exchange constituted as much gambling as betting on the point of an arrow at a roulette table?

Mr. BRUCE. Well, I do not know about that statement, but there was no question but that there was a period toward the height of that speculative period—and I think that the conditions were unsound—and could not definitely stay so. Where people paid 10 per cent for money to buy securities yielding 2 per cent. It could not go on. They knew they were gambling, of course, but everybody thought he was smart enough to get out ahead of the other fellow.

Senator GLASS. I had a chart prepared some time ago to indicate the period of time in which stocks passed on the New York Stock Exchange were held. The investigation disclosed that 12 years ago, the period was 67 days; that in recent years it had dropped to 22 days. Do you think people ordinarily invest their funds for 22 days?

Mr. BRUCE. No. I would hardly call that investment.

Senator GLASS. Nor I either.

Mr. BRUCE. But you seem to me to be trying by legislation to change human nature. I do not believe you could do it.

Senator GLASS. I would like to change some human nature, particularly my own.

Mr. BRUCE. So do all of us, but we can not.

Senator GLASS. We may restrain human nature, though, particularly the excesses of human nature.

Senator BULKLEY. Mr. Bruce, I think perhaps that goes a little too far. I think it may be difficult to change human nature, but is it not practical to restrict the use of Federal reserve funds? Isn't that what we are driving at? Isn't that what we should drive at?

Mr. BRUCE. I do not believe that you can segregate one part of the credit structure and put that off to one side and control that and leave the rest open. It is like a pool of water; you can not shove down one corner. It will come right up. You can go on now and try to restrict this class of loan and leave open the channels for borrowing money on other characters of security—

Senator BULKLEY (interposing). Yes.

Mr. BRUCE. And the money will find its way out and thru some channel will get back to be loaned on these same outlawed securities, if the public want to borrow on them.

Senator BULKLEY. We believe that we can restrict the use of Federal Reserve money for carrying speculative accounts, and we certainly intend to do so.

Mr. BRUCE. You can. The board can. It can increase its rates on all loans, and with the powers in that article 3, where a bank is going too far, where a bank is carrying too much of one security or carrying too many loans backed by one form of security, the Board can stop it, and they can do it quietly and the club will never have to be used as long as they have the club. I think they have the club now.

Senator BULKLEY. I think that would rather disprove the theory that it never has to be used as long as they have it, because there were certainly great abuses while the power still existed.

Mr. BRUCE. If they swing the club.

Senator BULKLEY. That is a pretty big "if." We never can be safe at that.

Mr. BRUCE. Well, can you? No matter what you do, can you?

Senator BULKLEY. We can do better than we have done.

The CHAIRMAN. We will have to, or we will not survive.

Senator GLASS. Mr. Bruce, I have here in my hand six pages containing 47 different paragraphs enumerating the powers of the Federal Reserve Board over member banks, and particularly the restraining power of the Federal Reserve Board over member banks. I am having prepared a paper showing the legislative restraints contained in the national bank act, which I apprehend will cover the same number of paragraphs, and I propose to put these in the record to show that this outcry against the centralization of authority to the Federal Reserve Board and restrictions upon what a member bank may do are not as valid as they would seem on the face of them.

(Thereafter Senator Glass submitted the following material for the record:)

CONTROL OVER NATIONAL BANKS UNDER REVISED STATUTES AND OTHER PROVISIONS OF LAW

Revised Statutes sections 5133 to 5156, both inclusive, regulate the organization of and confer certain powers on national banking associations.

Section 5136 enumerates the principal powers of national banks and confers power on the Comptroller of the Currency to redefine by regulation the term "investment securities."

Act of May 1, 1886, section 2: Change of name and place of business to be made only with the approval of the comptroller and not until comptroller has issued a certificate of approval.

Section 5137 limits the power of national banks to hold real property.

Section 5138 fixes the amount of capital necessary for the organization of a national bank and vests certain discretionary powers in regard to the matter in the comptroller.

Sections 5139 to 5143, both inclusive, embody provisions relating to the capital stock of national banks, the par value and transfer of shares, how they are to be paid for, how and under what conditions the amount may be increased or decreased, etc.

Act of October 15, 1914, the Clayton Act, sections 8 and 11, prohibit the existence under certain conditions of interlocking directorates between national banks, between a national bank and other member banks, and between national banks and any other banking association, and provide for the enforcement of the same.

Section 5151 imposes individual liability on the shareholders of national banks, and confers upon the comptroller the power to order closed any national bank whose surplus falls below 20 per cent of its capital.

Section 5155 provides for the retaining, establishment, and removal of branches of national banks, and confers upon the comptroller certain discretionary powers in the matter.

Sections 5157 to 5189, both inclusive, regulate the obtaining and issuing by national banks of circulating notes, and confers certain broad powers on the comptroller in the administration of such provisions and regulations.

Sections 5190 to 5219, both inclusive, provide regulations for the conduct of the banking business by national banks.

Section 5197 provides limitations on the rate of interest which national banks may receive or charge on loans or discounts, and section 5198 provides penalties for the violation of section 5197.

Section 5199 regulates the amount of dividends that may be declared by national banks.

Section 5200 limits the amount of loans that may be made to any one person, partnership, association, or corporation.

Section 5201 prohibits loaning on, or the purchasing of, shares of its own capital stock by a national bank.

Section 5202 imposes upon national banks a definite limit of the amount of indebtedness that may be incurred by them over and above certain excepted types of obligations.

Section 5203 restricts the use of circulating notes by national banks.

Section 5204 prohibits the withdrawal of any portion of capital by national banks during the continuance of banking business, and the payment of unearned dividends.

Section 5205 requires assessment upon shareholders of a national bank, upon notice by comptroller, in the case of a deficiency in capital stock.

Section 5206 prohibits the putting in circulation by any national bank of the uncurrent notes of any bank.

Section 5207 prohibits the holding of United States notes or national bank notes as collateral security.

Section 5208 makes unlawful the certification by any member bank of the check of any person, firm, or corporation, unless the drawer has on deposit with such bank an amount not less than that specified in the check, and providing penalties therefor.

Section 5209 provides penalties for embezzlement, misapplication, etc., of funds or credits of a Federal reserve bank or member bank by any officer, director, agent, or employer thereof.

Act of January 26, 1907. Prohibits contributions by national banks in connection with elections to political offices.

Section 5210 requires keeping of list of shareholders of a national bank open to inspection by the shareholders and creditors of the bank, and by the State tax assessors.

Section 5211 requires the making of reports by national banks to the comptroller and specifies the information to be contained therein, under oath or affirmation of an appropriate officer of the bank.

Section 5212 requires reports by national banks to the comptroller of the amount of any dividend declared, within 10 days after the declaration thereof.

Section 5213 provides penalties for failure to make the reports required under Revised Statutes, sections 5211 and 5212.

Section 5214, and act of March 14, 1900, section 13, require taxes to be paid to the Treasurer of the United States by national banks.

Sections 5215 and 5216 require semiannual returns for the purpose of assessing taxes made by national banks of the amounts of notes in circulation, and provides penalties for failure to do so.

Sections 5217 and 5218 provide for the enforcement of taxes and refunding of excess taxes.

Section 5219 allows State taxation of shares of national banks.

Sections 5220 and 5242, both inclusive, contain provisions governing the procedure on dissolution of national banking associations.

Section 5220 provides for a vote of the shareholders owning two-thirds of the stock of a national bank in order to effect a voluntary liquidation.

Section 5228 requires a national bank to cease the business of banking on failure to pay any of its circulating notes as ascertained by the comptroller.

Section 5234 gives broad discretionary powers to the comptroller in the appointment of receivers to take over the affairs of national banks which are in default, and prescribes the duties of such receivers, which are to be exercised under the direction of the comptroller.

Section 5236 regulates the distribution of the assets of an insolvent bank by the comptroller.

The acts of June 30, 1876, and March 29, 1886, both contain regulatory provisions of a similar nature.

Act of November 7, 1918, regulates the consolidation of national banking associations.

Act of February 25, 1927, Section 1, regulates the consolidation of State banks with national banks.

CONTROL OVER NATIONAL BANKS UNDER THE FEDERAL RESERVE ACT AND THE NATIONAL BANK ACT

FEDERAL RESERVE ACT

Section 2: National banks required to subscribe for capital stock of reserve banks up to 6 per centum of their paid-up capital and surplus.

Section 4: Discounts, advancements and accommodations to be extended to member banks by Federal reserve banks "subject to the provisions of law and the orders of the Federal Reserve Board."

Section 5: Additional subscriptions to capital stock of Federal reserve banks required of member banks when they increase their capital stock and surplus.

Shares of stock of reserve banks held by member banks not to be transferred or hypothecated.

Member banks required (1) to surrender proportionate amount of stock of reserve banks when the capital stock of member banks is reduced, and (2) to surrender all of their holdings of such stock when they voluntarily liquidate.

Payment for stock so surrendered to be made under regulations of Federal Reserve Board.

Section 6: Where receivers are appointed for national banks the stock held by them in reserve banks to be paid for under regulations of the Federal Reserve Board.

Section 11: Federal Reserve Board authorized—

(1) To examine member banks and to require such statements and reports as it may deem necessary.

(2) To suspend reserve requirements for 30 days with renewals of 15 days, and to fix a graduated tax upon the amounts by which such requirements are permitted to fall below specified levels.

(3) To add to the number of reserve and central reserve cities.

(4) To grant special permits to national banks to act as trustees, executors, and administrators and in other fiduciary capacities.

Funds deposited or held in trust by the bank awaiting investment not to be used unless securities approved by the Federal Reserve Board are first set aside in the trust department of the bank.

Surrender of fiduciary powers of a national bank is subject to approval of Federal Reserve Board.

Federal Reserve Board is authorized to make such regulations as it deems necessary with respect to the exercise by national banks of their fiduciary powers.

Federal Reserve Board was given power for temporary period (until October 31, 1921), upon the vote of not less than five members, to increase the amount of paper indorsed by any one borrower which Federal reserve banks could discount for any member bank.

Sec. 13. Reasonable charges by member banks for collection or payment of checks, drafts, etc., "to be determined and regulated by the Federal Reserve Board but in no case to exceed 10 cents per \$100 or fraction thereof."

Federal Reserve Board given the power to "determine or define the character of the paper thus eligible for discount within the meaning of this act."

The discounting or purchase of certain bills of exchange payable at sight or on demand to be "subject to regulations and limitations to be prescribed by the Federal Reserve Board."

Acceptance powers of member banks are limited generally (1) to an amount equal to 10 per cent of its paid-up and unimpaired capital stock and surplus for any one person, company, firm, or corporation, and (2) to a total amount equal to 50 per cent of its paid-up and unimpaired capital stock and surplus. The Federal Reserve Board, however, "under such general regulations as it may prescribe" may authorize any member bank to accept to an amount not exceeding 100 per cent of its paid-up and unimpaired capital stock and surplus.

Advances to member banks on 15 day paper to be at rates established by the reserve banks, "subject to the review and determination of the Federal Reserve Board."

Section 5202 of the Revised Statutes fixes the limit of the indebtedness of national banks at any time (except on account of demands of certain specified

kinds) at an amount not to exceed the amount of their capital stock actually paid in and remaining undiminished by losses or otherwise.

The discount and rediscount and the purchase and sale by reserve banks of bills receivable, domestic and foreign bills of exchange, and acceptances "shall be subject to such restrictions, limitations, and regulations as may be imposed by the Federal Reserve Board."

National banks may act as agents for insurance companies in certain cases "under such rules and regulations as may be prescribed by the Comptroller of the Currency."

Member banks may accept drafts or bills of exchange having not more than three months' sight to run, drawn "under regulations to be prescribed by the Federal Reserve Board" by certain banks for the purpose of furnishing dollar exchange. Such drafts or bills may be acquired by the reserve banks "in such amounts and subject to such regulations, restrictions, and limitations as may be prescribed by the Federal Reserve Board." The maximum limits of the acceptance powers of member banks are also specified.

Section 13a: The discounting by reserve banks of agricultural paper indorsed by member banks is "subject to regulations and limitations to be prescribed by the Federal Reserve Board."

The board may also, by regulation, limit to a percentage of the assets of a reserve bank the amount of paper which may be discounted and rediscounted by the reserve bank.

Section 14: Open market transactions of the reserve banks are subject to rules and regulations prescribed by the Federal Reserve Board.

The rates of discount to be charged by the reserve banks for each class of paper are also "subject to review and determination of the Federal Reserve Board."

Section 16: "The Federal Reserve Board shall, by rule, fix the charges to be collected by the member banks from its patrons whose checks are cleared through the Federal reserve bank * * *."

Section 18: Retirement of circulating notes of member banks is under the supervision of the Federal Reserve Board.

Section 19: Reserve requirements of member banks in the outlying districts of reserve and central reserve cities may be changed upon the vote of five members of the Federal Reserve Board.

Reserve balances of member banks may be checked against and withdrawn for the purpose of meeting existing liabilities, "under the regulations and subject to such penalties as may be prescribed by the Federal Reserve Board," but no bank shall make any new loans or pay any dividends unless and until the total balance required by law is fully restored.

Section 21: National banks to be examined at least twice each year "and oftener if considered necessary" by examiners appointed by the Comptroller of the Currency.

Expense of examinations to be assessed against the banks examined.

Special examinations of member banks by Federal reserve banks, with the approval of the Federal reserve agent or the Federal Reserve Board. Expenses of such examinations may, in the discretion of the Federal Reserve Board, be assessed against the banks examined.

Section 22: Prohibitions against loans by member banks to bank examiners, against purchases from or sales to their directors except in the regular course of business, etc.

Federal Reserve Board is given power by regulation to require full disclosure of the facts with respect to all sales of securities to a member bank by any of its directors or by a firm in which any such director is a member.

Section 24: Limitations are imposed by this section upon real estate loans by national banks and upon the interest rate they may pay upon time and savings deposits.

Section 25: The establishment of foreign branches by national banks must be approved by the Federal Reserve Board, which is also given wide discretion in connection with the examination and operation of the foreign branches which it authorizes. The board may also authorize interlocking directorates in such cases without regard to the Clayton Act.

Section 25 (a): Limitations are placed upon the amount of stock which national banks may hold in corporations formed by engaging in international or foreign banking in dependencies or insular possessions of the United States.

Officers of member banks may serve as officers of such corporations with the approval of the Federal Reserve Board without regard to the Clayton Act.

Section 27: National banks are taxed upon their circulating notes secured otherwise than by bonds of the United States.

Section 28 (amending section 5143 of the Revised Statutes): Reduction of capital stock of national banks must be approved by the Comptroller of the Currency and the Federal Reserve Board.

Mr. BRUCE. Senator, may I say—

Senator GLASS (interposing). Anything you please.

Mr. BRUCE. It seems to me a lot of your objectives throughout this bill might become more practical if you had control of all the banks, of all the banking facilities. But you have such a large amount of banks outside of your system that you do not control, and if you restrict too much the member bank and not those outside credit just runs around the corner to find its level. If there is cheap money anywhere on any collateral it will find its own level, no matter what you say to the member banks about special collateral loans.

Senator BARKLEY. Haven't you put your finger on one of the fundamental difficulties in our banking system?

Mr. BRUCE. I think so. You control only a part of the banking system.

Senator BARKLEY. What can we do about it?

Senator GLASS. We thoroughly realize that. Can you suggest to us what we can do?

Mr. BRUCE. No, sir. That is why I asked your permission to make that observation.

Senator WALCOTT. You have made a study of unified banking?

Mr. BRUCE. Yes; I would like to see them all in the same boat. You have restriction here that I mentioned, such as the restriction on interest. Right across the street is a bank that pays $3\frac{1}{2}$ per cent. You restrict me to 3 per cent. Who is going to get the deposits?

Senator GLASS. There are innumerable statutory restrictions on interest, are there not? Does not the State of Maryland put a limitation upon your charges for discounting?

Mr. BRUCE. I am talking about interest on deposits.

Senator GLASS. I know you are talking about your restraining power and you are talking about the other.

Mr. BRUCE. I know, but I am talking about the one that hurts. I am not talking about the other. I am saying that this would limit us to 3 per cent, and I think up to just a few months ago we were paying $3\frac{1}{2}$, everybody was paying $3\frac{1}{2}$.

Senator GLASS. Ought you to?

Mr. BRUCE. Now, if you would stop the savings banks and stop the State banks, I am all for it, yes, surely.

Senator WALCOTT. You are giving us arguments for a unified banking law, which, of course, we need very badly.

Senator BARKLEY. But how are we going to get it?

Senator Townsend. Mr. Bruce, what effect do you think this bill would have on the national bank system, the Federal system?

Mr. BRUCE. There is no use of saying you are going to break up the system, because you are not. I know of one right large trust company that was seriously considering, and even I might say negotiating, to come into the system, and since this bill has been introduced it certainly has backed away. Now that is just an illustration. I think that some situations will be such that some banks will have

to get out of the system. There is no doubt about it. There is a handicap if this bill does stand as drawn. It seems to me there is a handicap to the free competition with a nonmember bank. That means, I think, you will stop accretions to the system and you will have some leakage from it and you will have to stop those leakages, and you will right the ship by repeal of legislation and you will bring it back again to the present equilibrium. It certainly is not going to make membership more desirable.

Senator GLASS. That is what we have it designed to do, to make it more desirable.

Senator TOWNSEND. It was certainly considered by every member of the committee, I think, that the bill should make it more desirable to bring in banks that are not now in the system.

Mr. BRUCE. Well, you take the segregation of assets back of savings deposits; that is going to hurt, particularly where the savings of borrowing banks run to a high percentage. I heard of an instance in the last few days where a bank had 80 per cent of its money on time and it was loaning it around to farmers and generally local business about the neighborhood. What are they going to do here. They have got to call those loans and go back and invest it in real estate or savings bank securities that you specify. That certainly is going to be a handicap to that member.

The CHAIRMAN. May I ask you: Will that provision affect the larger banks less than it will the smaller banks?

Mr. BRUCE. Yes. Yes, very much. The particular bank I am connected with I do not think will be affected seriously. I think it is a very big debatable question about that segregation of assets. I mean I can make quite an argument on either side. Right now I just picked out the thing that I think is bad, the thing that is going to upset credit. I know what you are after, and in some ways there is considerable of it, but right now it is going to be had, and particularly to the little bank that has got a lot of money on time. What is he going to do? He is going to call the loan. He is going to or get out of the system.

The CHAIRMAN. You have the same view as Mr. Meyer had on that?

Mr. BRUCE. My examination of his statement was hurried, in a car this morning, so I do not know it thoroughly.

Senator BARKLEY. Mr. Bruce, what per cent of the deposits in the country banks, in your judgment, are time deposits?

Mr. BRUCE. I do not know. I know some instances. I have been told instances where they run up to 70 and 80 per cent. I know instances where they are 50 or 60 per cent.

Senator BARKLEY. As much as 75 per cent?

Mr. BRUCE. I do not know myself.

Senator GLASS. Mr. Bruce, how many banks, if any, of the 4,000 that have failed in the last two years, would you say failed because of the present condition of their portfolios?

Mr. BRUCE. I do not know. That is why they failed. They were frozen. They would keep on paying if they were solvent.

Senator GLASS. They failed because of the investments in unliquid securities?

Mr. BRUCE. Well——

Senator GLASS. Largely in real estate, was it not?

Mr. BRUCE. Their investments in securities depreciated to such a point that the sale of them did not give them enough money to pay their depositors in many instances.

Senator GLASS. Did they not have many on hand they could not sell at all?

Mr. BRUCE. The market got to such a point that a good many securities fell into that classification.

Senator GLASS. Do you think it is good banking to fill a bank's portfolio with investment securities that can not be realized on in an emergency?

Mr. BRUCE. Senator, you have gone thought a situation on which I do not believe you can draw conclusions for all time. I sat with a group of bankers on October 5, I think it was, one night until about 11 or 12 o'clock. My bank was in pretty good shape, but we all felt that if something did not happen this whole credit situation was going to close up, the way things were going. You could not sell anything. There was no price on anything. There was difference of opinion between us, whether it was going to happen in two days or four days. And then they brought out the National Credit Association, which gave everybody hope, and it started up again.

Senator GLASS. For 48 hours; yes.

Mr. BRUCE. Well, it lasted about four or five weeks and then down it went; and then you brought out the Glass-Steagall bill and the reconstruction act, and everybody took more hope. Now, if this proposed bill is going to unsettle matters and bring about uncertainty and make holders sell these securities to get inside the provisions of this law, you are going to depress all securities. Nobody can say what causes that depression except fear.

Senator BROOKHART. Is not the real trouble the fact that those securities are still inflated, still too high?

Mr. BRUCE. Well, if they are, I hope they will be a little more so for a while. [Laughter.]

Senator BROOKHART. The psychology of this thing is more inflation.

Mr. BRUCE. It is all psychology. There is nothing in the world that would do this country more good right now than a little inflation.

Senator BROOKHART. It is that question of making folks believe there is a value when there is no real value. I have a chart of the Federal Reserve Board that shows those securities up to date to be some 30 or 40 per cent higher than they were in 1914, and that was 33 per cent over the preceding level. That was too high. Now, commodities have gone way down below the 1914 level, but your securities are still up in the air. Is that a sound condition, or have we got to squeeze all the water and wind out of those securities before we get to a sound basis?

Mr. BRUCE. I do not know. I can discuss at length how we got where we are, but when you talk to me about how you get out of it, I say I have not seen anybody yet who can say; but I do know the first thing is to create an atmosphere of confidence. There is a tremendous amount of psychology about it.

Senator BROOKHART. About getting out, what would you say to this: If we would provide a set-up of a couple of billion dollars

or so, it would give the farmers a cost-of-production price for their products, they being a third of the buying power of the American people, and it would employ these seven or eight million people that are out of jobs. Would not that start things upward on a substantial basis?

Mr. BRUCE. I do not believe there is any substitute for the law of supply and demand. If there are more farm products than there is demand for them, their prices will be low. I do not believe you can pick yourself up by your bootstraps.

Senator BROOKHART. Do you not know that there is really no surplus of farm products at all; there is an underconsumption?

Mr. BRUCE. Well, that is what I mean. What is the difference between underconsumption and overproduction?

Senator BROOKHART. Would not that plan remedy the situation?

Mr. BRUCE. I do not know.

Senator BROOKHART. If we put these men to work?

Mr. BRUCE. I do not think so.

Senator BROOKHART. And remedy this thing at the bottom instead of at the top?

Mr. BRUCE. If we can change the atmosphere and let people once get the idea we are at the bottom of this thing, that it has spent itself, and there is some hope—then you will pick up.

Senator BROOKHART. In other words, you want people to again believe in securities that are still enormously inflated?

Mr. BRUCE. I do not admit they are still enormously inflated.

Senator GLASS. At all events, I am very glad that you believe in the Federal Reserve Board's proposed substitution for section 3.

Mr. BRUCE. It has that power now.

Senator GLASS. I think so, too, Mr. Bruce, but it has never exercised it.

Senator FLETCHER. Is not what is really needed an increased purchasing power of the people?

Mr. BRUCE. Of course it is.

Senator WAGNER. The way to do that is to put people back to work.

Mr. BRUCE. Yes.

Senator FLETCHER. It might be offensive to the bankers to suggest whether or not to do that might increase the supply of primary money.

Mr. BRUCE. I am not primarily a banker, but I know of a good many instances of corporations with which I am affiliated whose managements have said, "How much longer is this going to last?" They have opportunities for spending money for improvements. They are not doing it. They are afraid to do it. But the moment you get a feeling that this deflation has spent itself and that we are at the bottom, everything will begin to emerge.

Senator GLASS. Do you think it is good psychology to have bankers sit around a table and tell you that if you legislate at this time at all the whole banking system of the country will be wrecked?

Mr. BRUCE. I do not think it is good psychology, but I do not know what else they can say when they feel that the enactment of this is going to injure the interests they represent.

Senator GLASS. It is not simply that. Most of them have said that any legislation at this time will create such despair in the country that the banking system will be wrecked.

Mr. BRUCE. It may not be good psychology, but I do not blame them if they felt that way.

Senator BROOKHART. You said we have to restore the buying power of the people. The farmers make up more than a third of the American people. There is no way to restore their buying power but to give them a better price for their products, is there?

Mr. BRUCE. I did not say anything about buying power.

Senator BROOKHART. Yes; that was one of the comments in answer to Senator Fletcher.

Mr. BRUCE. That is true.

Senator BROOKHART. There is no way to give these seven or eight million unemployed men buying power but to give them jobs, is there?

Mr. BRUCE. No.

Senator MORRISON. There is no way to give them jobs except to make the industries they have been employed in more profitable.

Mr. BRUCE. Give them confidence that they are not going broke and they begin to spend money and move out again.

Senator MORRISON. You think we could more likely give employment to the unemployed by making industry profitable instead of doing it with Government donations, do you not?

Mr. BRUCE. Absolutely. I am not going into that.

Senator MORRISON. I know. I just thought I would ask you.

Mr. BRUCE. I do not want to go into that.

Senator BROOKHART. Industry itself has made itself unprofitable in these methods. It has brought this thing on. The farmers and the laborer and the people did not bring that on. You do not claim that?

Mr. BRUCE. No; but punishment is not going to bring them out of it. They have got to come out of it.

Senator BROOKHART. We passed a Bolshevik bill here with \$2,000,000,000 for the use of the banks and railroads. If we were to do as much as that for the farmers and the laboring people and restore their buying power, would not that have a substantial effect, whereas this other stuff is still psychology?

Mr. BRUCE. I would rather not go into that field. I have tried to study this bill and its effect, but I am getting right far afield.

The CHAIRMAN. If you have finished we will call the next witness. We are getting behind our schedule a good deal. I thank you very much.

Senator MORRISON. Mr. Chairman, I would like to ask a question if I may.

The CHAIRMAN. Pardon me. Go ahead.

Senator MORRISON. Mr. Bruce, as you interpret this bill it will give the Federal Reserve Board powers to control the administration of the assets of the banks belonging to the system further than they now have, will it not?

Mr. BRUCE. I would answer both yes and no. I think that they have hidden away in the provisions of the law a tremendous amount of power that they have not exercised. It has increased their power; yes. I would say it has.

Senator MORRISON. It makes clear that, in addition to the paper eligible for rediscount, they may say before they rediscount that you must do so and so about securities other than eligible paper, and they will control it more than they do now.

Mr. BRUCE. Yes.

Senator MORRISON. This additional power is not confined to stock-exchange collateral alone, is it?

Mr. BRUCE. Well, it is pointed more definitely at stock-exchange securities. In general terms it says so.

Senator MORRISON. The Federal Reserve Board in section 3 says: may prescribe regulations further defining and regulating the use of the credit facilities of the Federal reserve system within the limitations of this act. Such facilities shall not be extended to member banks for the purpose of making or carrying loans and other investments or facilitating the carrying of or trading in stocks, bonds, or other investment securities.

Just how do you define that expression, "investment securities?" What does that mean?

Mr. BRUCE. I think actually it is a very broad term.

Senator MORRISON. "Investment security?"

Mr. BRUCE. If you get back to the dictionary I think you will find that is a very broad term. In one section of the country it is interpreted to mean stocks and bonds, and in another section it covers warehouse certificates, and in another, mortgages.

Senator MORRISON. Mortgages on real estate?

Mr. BRUCE. Mortgages on all sorts of things.

Senator GLASS. Mr. Bruce, are you aware of the fact that that has been in the law for 19 years?

Mr. BRUCE. No, I am not. I have not touched on that. I do not dispute it. I just do not know it.

Senator GLASS. I say, you are aware of the fact that that requirement has been in the law?

Mr. BRUCE. I will admit it.

Senator GLASS. It has been in the act for nearly 19 years.

Senator MORRISON. Mr. Chairman, I do not want to collide with the Senator. It is not a very safe thing to do. But I was not through with the witness, and I would like to continue.

Senator GLASS. It does not make much difference if you collide with me. I just do not want anybody to collide with the law.

Senator MORRISON. I do not see, if it is in there, why you say that the fourth paragraph after paragraph 8 of section 4 of the Federal reserve act, as amended, is amended "by inserting before the period at the end thereof a comma" and so forth. It looks to me as though it is already in there, and it would not do any good to put it in again.

Senator GLASS. If the Senator will examine section 13 of the Federal reserve act, on page 29 of the latest print, he will see that the Federal reserve bank is not permitted to rediscount for any purpose except in the interest of agriculture, industry, and commerce.

Senator MORRISON. I am heartily in favor of that.

Senator GLASS. Let me finish, please.

Senator MORRISON. All right.

Senator GLASS. And that the board is very definitely denied the right in its definition of eligible paper to include notes, drafts, or bills covering merely investments issued or drawn for the purpose

of carrying on or trading in stocks, bonds, or other investment securities.

Senator MORRISON. I understand that; but now, before they rediscount this paper, which alone is subject to rediscount, you are giving them the power to say to that bank what they shall do with their funds, as I understand the law, and I think it is very clever, and you give them the power.

Senator GLASS. We are simply saying what a Federal reserve bank shall do.

Senator MORRISON. Yes, sir; but the law you read defines what notes they may rediscount, and I subscribe to that. That is all right. But I do not want, if I can help it, to give them the power to say, "Before we will discount that paper properly eligible, you shall run your bank as we tell you to with reference to other investments." I want to ask the witness to tell me if, in banking life, nearly all securities which are good and not short-term paper in business process is looked upon as investment paper.

Mr. BRUCE. Yes; if there is anything you can invest in.

Senator MORRISON. Would not this act, under the language I have read, give the Federal reserve system the power to say to any bank that belonged to the system, "Before we will rediscount your eligible notes, we direct that you rearrange your loans and put a greater proportion of them in paper other than investment paper"?

Mr. BRUCE. That is the intent, sir.

Senator MORRISON. If it is not, what is it? If that is not what it does, what does it do? Do you think that is a wise power to give this central board?

Mr. BRUCE. I think in effect it has that power in broad terms now.

Senator MORRISON. Fortunately for the country they have not thought so. They only used moral suasion.

Mr. BRUCE. By moral suasion, one way or another, they could come to a bank and the examiner would say to a bank, "You are loaning too much money on that particular security. Before we come back for our next examination, we want you to shift that around and get a more diversified list of collateral back of that loan." That is what they do.

Senator GLASS. The courts have decided the board has that right now.

Mr. BRUCE. I did not know that, but I know they do it, and I know we do it, too, when they tell us to, if we can.

Senator MORRISON. Yes; and if they have that power now—

Mr. BRUCE. I do not know whether it is legal or not.

Senator MORRISON. Can you point out to me what law it is under?

Mr. BRUCE. I do not know. I said it may be moral power. I can not answer you. I can not stand examination on the Federal reserve law.

Senator MORRISON. My information is, they do it and have been doing it.

Mr. BRUCE. They do it.

Senator MORRISON. That is one of the biggest troubles of this country to-day, in my opinion. What percentage, generally speaking, would you say of the banks of this country were eligible for discount under that law?

Mr. BRUCE. It has decreased very much. I do not know the percentage. It is very small. It has been decreasing in the past 10 years, because the method of doing business has been changing. The companies, that used to do business by seasonal borrowing, during the period of prosperity have been able to issue securities and supply themselves with money, they they are not borrowing. Therefore the amount of eligible paper has decreased from this cause. And then, of course, in this time of depression there is not the same activity of business. It has gone down. I do not know what it is. I know it has decreased.

Senator MORRISON. Could you form an opinion satisfactory to yourself, an estimate, of the percentage of the whole banking?

Mr. BRUCE. No. I do not know.

Senator MORRISON. Well, it is small, is it not, the country over?

Mr. BRUCE. I just do not know. I think it is small; yes.

Senator MORRISON. Do you not think there is danger of attaching too much importance to this small percentage of the small types of credit in the country and too little to the larger types?

Mr. BRUCE. I think that credit is credit and it is fluid. I do not believe you can crucify one end of it, constrict one end, for it will slip up and come around on the other side, particularly when you have a lot of banks that are not in the Federal reserve system.

Senator MORRISON. You could not run the banks in this country on only eligible paper?

Mr. BRUCE. Oh, no. What are you going to do with your money? You have got to put your money somewhere. What are you going to do with it?

Senator MORRISON. Do you think that banks could invest it as wisely as Government officials could tell them to invest it?

Mr. BRUCE. I think the bank ought to have just as much autonomy as it is possible to leave with them without wrecking somebody else.

Senator MORRISON. That is all I have to ask.

Senator GLASS. Do you think the Federal reserve system in its administration has deprived the banks of autonomy?

Mr. BRUCE. No.

Senator GLASS. Do you see any difference, Mr. Bruce, between commercial banking which requires always liquid assets to pursue its activities and investment banking?

Mr. BRUCE. Do I see a difference?

Senator GLASS. Yes.

Mr. BRUCE. Of a degree.

Senator GLASS. Well, I say a difference.

Mr. BRUCE. Yes. A difference of degree; yes.

Senator GLASS. What I am trying to get at is whether you think the requirements of existing law are too restrictive as to the eligibility of paper for discount at Federal reserve banks.

Mr. BRUCE. Senator—

Senator GLASS. In other words, would you freeze up the portfolios of the Federal reserve banks just as the portfolios of thousands of banks throughout the country are frozen up?

Mr. BRUCE. No. We want the security back of our currency as liquid as possible in normal times. Right now we are in a position—we will not go into that.

Senator GLASS. I anticipated your answer.

Senator FLETCHER. How do your time deposits compare with your demand deposits, Mr. Bruce?

Mr. BRUCE. I think our time deposits are a little less than half. About 40 per cent.

Senator BARKLEY. Has there been any falling off in the time deposits over a period of, say, two years due to the widespread fear among a lot of our people about our banking situation?

Mr. BRUCE. Oh, yes.

Senator BARKLEY. They hesitate to tie up their funds in long-time deposits when they might want to get them out to-morrow.

Mr. BRUCE. Yes. There is a lot of money tied up to-day. If they had a little assurance they would go right over in time deposits.

Senator BARKLEY. Let me ask you this: This is not assuming anything that the committee will do, but assuming that it should look with favor on the suggestions of the Governor of the Federal Reserve Board with reference to amendments to this bill, would you still say it would be unwise to enact legislation now?

Mr. BRUCE. I have said right clearly, I think, I do not want to see anything enacted if it is open to the suspicion of causing more liquidation of securities. I think you can pick out different things in this bill that are all right; but I think the things that change the present flow of credit and the present holdings of securities, that are going to shift them around, are going to have a disturbing effect and are going to retard what I am looking for, and that is a feeling of confidence.

Senator GLASS. If they really do that.

Mr. BRUCE. Well—

Senator BARKLEY. If we may assume that there are some fundamental defects which we found out from experience in our present banking situation, we can attempt to remedy them.

Mr. BRUCE. Oftentimes a patient is right sick, you know, and he needs some violent medicine, but you have to build up his constitution before you can administer it; and if you can tell me how long the depression is going to last, then I can approach it. We are still sliding and there is not yet any stabilization or turning up of business. I think it is a bad time for applying strong medicine.

Senator GLASS. Mr. Bruce, you are a well-informed man.

Mr. BRUCE. Thank you.

Senator GLASS. Can you tell us when, if ever, a bank reform measure has ever been passed except after a financial debacle?

Mr. BRUCE. Senator, I think I am right. The Federal reserve bank act came into being as a result of the panic of 1907.

Senator GLASS. And 1908?

Mr. BRUCE. And 1908. That started, I think, the movement for the formation of the Federal reserve system, and seven years elapsed before we passed it.

Senator GLASS. Oh, no; not seven.

Mr. BRUCE. In 1914.

Senator GLASS. 1913?

Mr. BRUCE. 1913. December 23, 1913.

Senator GLASS. Yes. But all that time we were trying to do something.

Mr. BRUCE. All right, keep on trying. That is all right. Let us keep on. But let us not do it right now. Let us not do it in the middle of this depression.

Senator GLASS. As a somewhat experienced legislator over a period of 30 years in Congress, my conclusion is unless you do it now you will wait to have another such lesson as we have had recently to ever do it.

Mr. BRUCE. Senator, we start from one different premise. I think this depression is unprecedented in the history of the world. It is something that people who usually are able to find a logical reason and reach a conclusion do not know. I think this depression is different.

Senator GLASS. The Comptroller of the Currency, for example, thinks the adoption of branch banking would do something.

Mr. BRUCE. That is all right. I have no objection to that.

Senator GLASS. That is important legislation and is a bitterly controverted proposition.

Mr. BRUCE. I limit my objection to just those parts that are open to the suspicion of causing more liquidation and disturbance.

Senator GLASS. Of course, if we could be convinced—as some of us have been—that any provision of this bill causes that, we would modify or eliminate it.

Mr. BRUCE. You tell an affiliate his parent bank can not loan more than 10 per cent of its capital stock and surplus. A lot of them have more than that. What is he going to do? He is going to sell to get within the law.

Senator GLASS. You mean affiliates?

Mr. BRUCE. Yes.

Senator GLASS. We had pretty high authority for the abolition altogether of affiliates of national banks. We brought here some of the most experienced and enlightened practical bankers in the United States, who advocated abolition of them, and two of these bankers told us they had already abolished their affiliates.

Mr. BRUCE. Senator, I am not going to argue with you about that at all. I know that affiliates have sprung up like mushrooms during the last 10 years, for all kinds of purposes. It is a back door to banking, and I think they ought to be controlled. But I am not going to argue with you. Maybe some of them ought to be prohibited. I do think right now is a right bad time to break up the equilibrium.

Senator GLASS. How about three years from now?

Mr. BRUCE. If you will tell me how long the depression will last, I will give you an opinion. I do not know.

Senator GLASS. If you will tell us how long, we will adapt ourselves to that.

Mr. BRUCE. You are still in session. You come back here every year.

Senator WAGNER. What has been the experience of your bank during the last 12 months? Has there been a shrinkage in the amount of loans made by your bank?

Mr. BRUCE. I came into a bank only about six months ago and I came in at the end of a right strenuous period, and since that time, by hook or crook, we maintained a stability of our deposits. I am not a banker in any sense.

Senator WAGNER. What I had in mind was whether there was a demand for credit facilities now, or whether the demand had decreased.

Mr. BRUCE. The demand for commercial notes has decreased with the decrease in the activity of commercial transactions. It has decreased a great deal.

Senator WAGNER. It is a controversial question as to whether the shrinkage in outstanding loans has been caused by a lack of demand for credit or by a refusal of the bankers to extend it.

Mr. BRUCE. In my bank, in repeated instances, the line of credit which we give to various enterprises has, with the consent or at the suggestion of the borrower, been reduced because they do not need it. I mean the demand, of course, for money has decreased with the decrease in the amount of money in current assets of the going concern. As that decreases, the money tied up decreases. It has decreased.

Senator MORRISON. Mr. Bruce, there has not been very much trouble at any time about loans by the banks on sound paper eligible for rediscount, has there, because they could use that?

Mr. BRUCE. I do not think there has been any trouble to obtain such loans.

Senator MORRISON. Has there ever been any trouble?

Mr. BRUCE. No; I don't think there has been with that.

Senator MORRISON. And the trouble with the country was that as the depression grew, good paper did not have a resort for rediscount privileges, and that is why the demand for the Glass-Steagall bill came—that there might in an emergency be enlarged power?

Mr. BRUCE. Yes.

Senator MORRISON. Do you not think that legislation has tremendously helped the country?

Mr. BRUCE. Oh, absolutely; yes. I do not know what would have happened to us without that.

Senator MORRISON. Exactly; because we increase the rediscount power of the Federal Reserve Board.

Mr. BRUCE. Yes.

Senator MORRISON. And did not that tend to stop collections and foreclosures by the banks of noneligible paper?

Mr. BRUCE. It loosened up the whole credit. Absolutely.

Senator MORRISON. To let them realize there was a resort?

Mr. BRUCE. A hope.

Senator MORRISON. And prior to that they had to make collections?

Mr. BRUCE. Yes.

Senator MORRISON. And make their banks more liquid?

Mr. BRUCE. Yes.

Senator MORRISON. And that has, at least to some extent, increased throughout the country?

Mr. BRUCE. A very considerable extent.

Senator FLETCHER. Have you any affiliates, Mr. Bruce?

Mr. BRUCE. Yes, sir.

The CHAIRMAN. We would like to hear the next witness, because we have the afternoon full. Mr. Rand, will you come forward?

STATEMENT OF GEORGE F. RAND, PRESIDENT OF THE MARINE TRUST CO., OF BUFFALO, N. Y.

The CHAIRMAN. I suggest to the members of the committee if we are going to get through with our hearing in proper time they let the witness finish his statement first and then ask questions afterwards.

Senator GLASS. I will agree in advance.

The CHAIRMAN. You may proceed.

Mr. RAND. There has been so much discussion of the general provisions of the proposed bill that I am going to confine myself to the portions that would affect our group of banks in New York State, feeling that that could help the committee more than if I discussed the general legislation, which has been so ably discussed before.

Senator FLETCHER. Will you state what you represent?

Mr. RAND. I represent the Marine Trust Co. of Buffalo and the Marine Midland Corporation.

Marine Midland Corporation is a parent or holding company, organized under the laws of Delaware with an authorized capital of 10,000,000 shares of the par value of \$10 each, of which 5,550,768 shares are issued and outstanding. Of these, 1,000,000 shares were issued for cash at \$60 a share, less underwriting commissions, upon the organization of the corporation in October, 1929. The corporation, therefore, commenced business with \$57,285,236 in cash, of which it still holds upwards of \$19,000,000, the balance having been used in the acquisition of additional bank stock upon original acquisitions and upon recapitalization of several of the banks for the purpose of strengthening their condition; \$19,287,591.49 of this amount has been invested in Marine Midland banks as additions to their capital and surplus since the organization of the corporation. The corporation has no liabilities.

The remaining shares of Marine Midland Corporation stock, other than the 1,000,000 so sold for cash, were issued in exchange for shares of stock of the constituent banks and trust companies.

The group consists at the present time of 20 banks and trust companies, over 98 per cent of the stock of each of which, excluding directors' qualifying shares, is owned by Marine Midland Corporation.

The group also includes two security affiliates, Security Properties Co. (Inc.), 96.5 per cent of the stock of which is owned by Marine Midland Corporation and which is operated in connection with the bank at Troy, N. Y.; and Fitrust Corporation, 45.49 per cent of the stock of which is owned by Marine Midland Trust Co. of New York and 54.29 per cent by Marine Midland Corporation. Both of these companies are being liquidated and it is part of the plan on which the group is organized that they shall be dissolved as soon as conditions warrant.

Marine Midland Group (Inc.) is the service corporation. This was organized under the laws of New York with a nominal capital stock which is owned by the various banks in the group. Its officers furnish service and advice to the member banks through central auditing staff, central credit file, standardization of forms and accounting practices, bond investment advice, publicity, advertising, and new

business, and so forth. In this corporation all of the activities of the group as such are centered, the Marine Midland Corporation being merely a passive holding company, practically the sole business of which consists in receiving dividends on the bank stocks owned by it and interest on its bank balances and paying out its earnings in dividends. It has no liabilities.

Statements as of December 31, 1931, with map, showing location of the banks and statements of their condition on that date, together with combined statement of all the banks as of that date and lists of officers and directors, and copies of the annual report to stockholders covering the year 1931 are submitted herewith.

The past two years have seen the organization of the Marine Midland Corporation fully justified. Its organization has materially strengthened the banking structure throughout central and western New York. Through the medium of the cash resources, which it possessed, it has been enabled to contribute large sums of money and management to the banks in its group, which might otherwise have had great difficulty in raising additional capital.

The Marine Midland Corporation has also been very effective in its assistance to banks outside of the Marine Midland Group in working out their problems and in assisting them during this period.

In the management of the National Credit Association group No. 1, western New York, the Marine Midland group took a prominent part and its officers worked unselfishly in helping solve the problems of banks throughout the territory.

It is an interesting thing to me that so many group banking organizations, with practically no knowledge of each other, sprang up almost simultaneously in different sections of the country as the result of a distinct need for this type of banking. The northwest group, the Michigan group, Atlanta group, our group in western New York developed along very much the same lines, although entirely independent of each other and with no conferences and with no working together in any way. It seems to me that they fill a distinct need in our banking structure. Group banking, during the past two years, has been one of the most constructive features in our whole banking situation.

In the provisions of the new Glass bill we hope that the splendid work done by group organizations will be given recognition and encouragement and will not be penalized by burdensome restrictions.

I arrived last evening and had the privilege of reading Mr. Wakefield's statement to your committee yesterday. Mr. Wakefield's statement represents my views in many respects. I concur in his recommendations regarding section 20 in reference to the reserves in assets other than bank stocks to be accumulated by holding companies, in reference to branch banking contained in section 21, in reference to the reserve requirements for national and member banks contained in section 13, in reference to limitation of investments of time deposits contained in section 14.

The provisions regarding the reserves against time deposits would require approximately \$12,000,000 increased reserves to be carried by the member and national banks in our group; 5 per cent on this would be \$600,000 a year additional cost to us. This is a terrific burden of additional cost at this time. However, I do not think the additional cost should be the controlling feature, but I do feel that

the banks have operated on the present reserves and I do not think the reserve requirements are the cause of our banking difficulties.

The aggregate amount of time deposits in the national and member banks in our group December 31, 1931, was \$166,000,000.

In passing, I wish to point out that the provision governing the granting of a permit to vote stock of national banks held by a holding company should be amended so as to allow such a permit to apply to an officer, director or employee of such company and to provide that it shall include the right to vote the stock of national banks at all meetings of the shareholders and for all purposes rather than being limited as in the present bill to voting for directors.

Also, it is not provided in the bill how a national bank can operate and carry on its corporate existence if a majority of its stock is not allowed to vote. Many statutory provisions require the consent of a majority or two-thirds of stock and the effect of the prohibition would be to cause confusion in the corporate affairs of the bank.

In any event it is my opinion that the Federal Reserve Board should not be given arbitrary power to withhold or revoke such a permit. If the holding company complies with the conditions and provisions set forth in section 20 it should as a matter of right be allowed to vote the stock of national banks held by it.

Limitation of the right to declare dividends to the "actual net earnings" as determined by the comptroller might give rise to serious differences of opinion. It would seem to take away the discretionary power properly lodged in the board of directors.

I wish to call attention to one other provision, section 18 of the bill, which in my opinion has a much more far-reaching effect than popularly supposed. Under this provision, if literally construed, 71 directors now serving on the boards of our various banks would be disqualified, among whom are many of our most valuable directors.

In closing, I again refer to the constructive work done by our group in western and central New York, and in illustration I would like to cite two concrete instances. In Albion, N. Y., in Orleans County, 11 banks had closed their doors in 27 days, within a radius of 20 miles, including the Citizens National Bank of Albion, leaving our Orleans County Trust Co. the only operating bank in this vicinity. Within 2 months and 11 days of closing of the Citizens National Bank, we had made arrangements with the national banking department and had given immediate credit of 50 per cent to the depositors of the closed bank, which set a record for speed in liquidation in our territory. At the present time we are planning to open a new bank in Medina, a village of 6,000 population, where both banks have failed, and at the request of the banking department, we are organizing a new bank there, which will be opened about April 4, and will take over certain assets of the closed banks and give depositors of the closed banks credit for a proportion of their deposits. I cite these two instances, and these are typical, to show the constructive work we are doing, and I might say that rural New York State does not present essentially different problems from the other groups in the West and South.

In conclusion, I submit that the record made by group banks throughout the country, during the past two years, has demonstrated beyond doubt, the economic soundness of the principle upon which

they have been organized, and their right to recognition and encouragement in any new legislation.

Senator FLITCHER. Would you be pleased to have all your affiliates branches instead of affiliates?

Mr. RAND. Yes.

Senator WALCOTT. Mr. Rand, have you had the opportunity of studying the recommendations of yesterday? Have you seen them?

Mr. RAND. Of the Federal Reserve Board? No; I have not. I read it in the morning paper, but I have not had an opportunity to study it carefully.

Senator WALCOTT. Going back to branch banking versus group banking: Would you put a system of branch banking in States regardless of State laws?

Mr. RAND. Yes.

Senator WALCOTT. That is the only way to get started, is it not?

Mr. RAND. I do not think the national banking system should cater to each separate State. I should think they would have a uniform system of branches irrespective of State laws.

Senator GLASS. If we should do that, Mr. Rand, will you and these other gentlemen who have been here come down here and help us get it through?

Mr. RAND. Senator Glass, I will if I can. If I can be of any help I will be glad to do so. I can not answer for the other gentlemen, but I will.

The CHAIRMAN. I was just going to suggest that the witness says we might ignore State laws in banking. I might add to that that the Federal reserve law seems to have been pretty much ignored in the banking also. Go ahead, Senator Wagner. You were going to ask a question.

Senator WAGNER. I was going to ask about a local situation in Albion, where you say your group opened a bank.

Mr. RAND. We did not open a new bank. We had a bank at Albion, N. Y., a small bank, and within a period of a few weeks practically every bank in several counties was closed, and the other bank in Albion has closed. We immediately, as soon as we were able to do so, made an arrangement with the national banking department and gave immediate credit to the depositors of the closed bank to the amount of 50 per cent of their deposits with the closed bank in our bank, which was the only other bank in the town.

Senator WAGNER. Those credits were mostly agricultural, were they not?

Mr. RAND. No. We took over their bond account. We took over certain loans that they had that we thought were good. We took enough of the closed bank's assets to protect us for the advance we made.

Senator GLASS. Did they let you have them at the market price?

Mr. RAND. We took them at the market price, Senator.

Senator GLASS. You made money on the transactions, did you not?

Mr. RAND. We sold the securities right out. We did not gamble on the securities. We sold them out the day we got them except for the Government bonds and the New York State and municipal bonds.

Senator WAGNER. Is not there a need for more banks in that particular section?

Mr. RAND. The section had too many banks, as a matter of fact. Senator WAGNER. Have they now?

Mr. RAND. I am not prepared to say that. At one time in Medina, a town of six or seven thousand people, they had no banks, and we are opening a new bank there around the 4th or 5th of April.

Senator BARKLEY. Do you have any bank in your own city?

Mr. RAND. In our own city we have one, the Marine Trust Co.

Senator BARKLEY. Your group is largely country banks?

Mr. RAND. No. Our group is built up around the Marine Trust Co. of Buffalo, which is a \$250,000,000 bank, and we have a large bank in Rochester and a large bank in New York City, the Marine Midland Trust Co., which is a member of the New York Clearing House Association.

Senator GLASS. Mr. Rand, in a sense, then, and in a degree do we not have nation-wide branch banking in this country now?

Mr. RAND. Do we not have nation-wide branch banking?

Senator GLASS. In a sense and in a degree, through correspondent banks? In other words, does a bank in Chicago and various banks in New York have as many as 4,000 or 5,000 correspondent banks throughout the country? Is not that in a sense and in a degree branch banking?

Mr. RAND. No, I do not see, Senator Glass, how it is. It may be in some sense, in some degree.

Senator GLASS. That is what I am saying. In other words, the correspondent bank, usually the little country bank that has its correspondent in New York City or in Chicago or in St. Louis, is in a sense subservient to its big bank, is it not?

Mr. RAND. No; I would not say that, Senator Glass.

Senator GLASS. I know you would not, but I would.

Mr. RAND. The difference is that the New York bank has no jurisdiction over its investments.

Senator GLASS. It has not statutory jurisdiction over it, but it extends its privileges, does it not, for which it is duly thankful, or gives it advice, does it not, which it usually follows?

Mr. RAND. I would not say that. It will if it is asked for, probably. It depends on the local situation. But where a New York bank has several thousand correspondents, I do not see how it can take very much interest in the internal affairs of any one of those correspondents.

Senator GLASS. It does not extend privileges without knowing something about their business, does it?

Mr. RAND. I did not understand that question.

Senator FLETCHER. They do not really extend privileges; they require the correspondent bank to put up the money with them, do they not?

Mr. RAND. I am not qualified to answer on that.

Senator GLASS. I know, but the reason they put up the money is that they expect the privileges to be extended, and they are extended, and the little bank feels under obligation to the big bank.

Senator BROOKHART. There are times when the big bank allots investment issues to the little banks, and they usually take their allotment.

The CHAIRMAN. In confirmation of the statement of Senator Glass, I will say I have noticed that our small bankers in South Dakota, in conversation, will state, "I have just been down to Sioux City and talked with the big bankers, and so and so." When I am in Sioux City, they say, "We have just been to Chicago and we saw the Chicago banker." He says he has just been to New York City. Now, it seems where our banks were loaded with poor securities and we have talked to them, they say, "Why, yes. The Sioux City people say it is all right." The Sioux City people say they have talked with Chicago, and Chicago said it was all right. The Chicago people say they have talked with New York, and New York says it is all right. So I quite agree with Senator Glass that we have a branch banking system now, and, in my opinion, too much of it, and I think the condition of our banks in the country is proof of it.

Mr. RAND. I think we have the very opposite of that. The New York banks or the large city correspondents have no control over the purchase of securities or the investments of the smaller banks; and there are so many other agencies that are selling securities to the small bank that I think you will find the proportion of the securities sold to the correspondent banks by their New York bank correspondents is not high but very small.

The CHAIRMAN. We got information about certain ones that really had to buy securities. That is a different thing from buying voluntarily. They had allotments of other banks which were pushed out on them. At the time it seemed to be good. Now they know it is not good.

Senator GLASS. They may not have borrowed from the parent bank but from its affiliate.

Senator BROOKHART. Yes, that is the point.

The CHAIRMAN. May I ask one or two questions? I am not sure I understand your set-up clearly. How many banking units have you?

Mr. RAND. We have 20 banks.

The CHAIRMAN. Is their stock held by a holding company?

Mr. RAND. Their stock is held by a holding company.

The CHAIRMAN. Nearly all of that bank stock is held?

Mr. RAND. About 95 per cent and upward.

The CHAIRMAN. Do you retain the double liability on the holding company stock?

Mr. RAND. No, we do not. We are not against double liability. When we formed our company we raised \$50,000,000 in cash, which was more than the total double liability would be.

The CHAIRMAN. You are carrying your reserve in the holding company as a protection?

Mr. RAND. At the present time we have \$19,000,000 in cash in our holding company.

The CHAIRMAN. What is the total capital of your banks?

Mr. RAND. About \$32,000,000.

The CHAIRMAN. Thank you.

If there is no objection, the reporter will place in the record comments on the Glass bill submitted by the Wilmington Trust Co. of Wilmington, Del.

WILMINGTON TRUST Co.,
 Wilmington, Del., March 28, 1932.

Hon. JOHN G. TOWNSEND, Jr.,
 United States Senate, Washington, D. C.

DEAR SENATOR TOWNSEND: I shall inclose herewith comments upon the Glass bill. Its proposed treatment of securities and collateral loans is extremely objectionable to us in the Wilmington Trust Co. I hope you agree with me.

Yours truly,

HENRY P. SCOTT, *President.*

THE REVISED GLASS BILL, S. 4116, INTRODUCED MARCH 17

This is little better than the first Glass bill. It will force extreme deflation; restrict the independence of the Federal reserve banks and subject them to political control and to an open-market committee; discriminate against collateral loans further than now; discriminate against 15-day notes, the principal instrument of member bank borrowing; hamper the Treasury of the United States in financing its great requirements by charging discriminatory rates for loans to banks on Government securities; require increased reserves by member banks against time deposits; and require member banks to write down their real-estate assets and loans to present market values.

FEDERAL RESERVE BANKS

The Glass bill limits the powers of the Federal reserve banks and aggrandizes the Federal Reserve Board in Washington. This is probably in the long run the most dangerous feature of the bill, because it derogates from the autonomy of the banks and subjects them to political control. To say this is no reflection on the present Federal Reserve Board or the present exceptionally able governor thereof. It is a matter of principle that the Federal reserve banks should be autonomous banks, run by local bankers and supervised, but not operated by a board in Washington appointed by the President and confirmed by the Senate. Section 12 for instance provides that the Federal Reserve Board shall exercise special supervision and control over all relationships of any Federal reserve bank with any foreign bank or banker. This is only an instance. The bill bristles with infringements upon the autonomy of the Federal reserve banks.

NEUTRALIZING THE GLASS-STEAGALL BILL

Equally dangerous and perhaps more disheartening at this moment is the provision of section 10 to subordinate the open-market powers of the Federal reserve bank to an open-market committee, consisting of the Governor of the Federal Reserve Board and representatives of the 12 Federal reserve banks, acting at meetings to be held in Washington at least four times a year, by formal resolution, and subject to the approval of the Federal Reserve Board. This seems hopelessly cumbersome and dilatory procedure. The principal constructive significance of the recently enacted Glass-Steagall bill, upon which such high hopes were built, lay in the authority (a) to member banks having a capital less than \$5,000,000 to borrow on collateral security from the Federal reserve banks, and (b) in the authority of the Federal reserve banks to secure Federal reserve notes by United States Government obligations purchased in the open market. The revised Glass bill would overcome the constructive features of the Glass-Steagall bill by discriminating more than ever against collateral loans and by putting the Federal reserve banks' open-market powers into commission in such a way as to be unusable. The country thought it was to be saved from depression and deflation by the Glass-Steagall bill. Is the original Glass bill now to be revised to the end that depression and deflation shall continue in the land?

HAMPERING TREASURY FINANCE

In a period when the treasury of the United States has an unusually heavy volume of necessary financing, and after two failures of Treasury issues last fall, section 11 imposes a rate 1 per cent higher than the discount rate upon any bank that ventures to borrow on 15-day notes. This will imperil Treasury financing and depress bond prices. It is important to remember that member banks as a matter of convenience and a matter of course during 15 years have maintained a large holding of short Government paper as furnishing the most convenient kind of eligible paper and that there is a scarcity of other eligible paper in this depression period.

THE UNSOUND THEORY OF THE BILL

The theory of the revised Glass bill, like that held by the Federal Reserve Board in 1920, is that monetary control should be had, not by raising and lowering the discount rate, but by discrimination between borrowers or "direct action." Now, it is axiomatic that the function of a bank of issue is to control the price and volume of credit and that the credit which it creates will flow along natural channels where it is wanted to the highest bidder. Credit is like water, or, even more, like quicksilver, and it follows its natural course. However, the Federal Reserve Board in Washington during the inflation period held the contrary view and attempted to put it into practice. It prevented the Federal reserve banks from raising the discount rate and attempted to ration credit to the stock exchanges and call money market, with what disastrous results we know.

It will be recalled that the consequence was that the call-money market was obliged to pay very high rates for money, and that these very high rates attracted loans "from others" and from all over the world. They did not discourage but rather stimulated speculation. The bull market continued unabated, and, indeed, activity was exaggerated all through the first half of the year 1929 and until after, in August, 1929, the Federal reserve banks were finally permitted by the Federal Reserve Board to increase their discount rates. That stopped it instantly.

This was to be expected. It is not possible to inflate business and agriculture with cheap money and cheap credit and at the same time to induce people, by admonition or restriction or rationing, not to buy securities which the inflation is making attractive. The orthodox remedy for inflation is to raise the discount rate, not to deny credit to honest borrowers on good security.

But the revised Glass bill proceeds on the unsound and vicious principle of "direct action" advocated and tested by the Federal Reserve Board in 1928 and 1929 with such disastrous consequences to the country. The bill attempts to outlaw investment securities, the owners of them, dealers in them and banks that lend on them. The country as a whole is to be punished for the inflationary excesses of 1927 to 1929 by being subjected in 1932 to a further drastic deflation of securities and of credit.

The bill undertakes to provide that the boom, which ended in September, 1929, shall never happen again. So preoccupied is the bill with preventing the recurrence of the boom that it has set up machinery well devised to perpetuate and aggravate the depression.

The Federal reserve act never has, until the Glass-Steagall bill, permitted the Federal reserve banks to lend money to member banks on investment securities or on other securities than on eligible paper, and governments. However, it is the bill's purpose to go further and, so far as practicable, control all the assets of every member bank and restrict their use in collateral loans. So far as practicable, the entire resources of all the banks are to be controlled by the Federal Reserve Board to suit the theory that stocks and bonds are bad, that people who borrow on them are bad, that banks that lend on them are bad, and that Congress, by law, can control the use of the whole of the assets of the banks to suit this theory.

Thus a principal feature of the bill is to force banks to discriminate against collateral loans on stocks and bonds. Through control of the lending power of the Federal reserve banks it is proposed to control, not only the money lent by them, but also all the assets of the member banks.

PROVISIONS AGAINST OWNERS OF INVESTMENT SECURITIES AND DEALERS IN THEM
AND BANKS THAT LEND ON THEM

Section 3 authorizes the Federal Reserve Board in Washington to prescribe legislation further defining and regulating the use of the credit facilities of the Federal reserve system. The section provides that such facilities shall not be extended to member banks for the purpose of making or carrying loans covering investments, or facilitating the carrying of, or trading in, stocks, bonds, or other investment securities other than obligations of the Government of the United States. Each Federal reserve bank shall keep itself informed of the loan and investment practices of its member banks and the uses made by them of the credit facilities of the Federal Reserve System. The chairman, who is the agent of the Washington board (not the governor, who is the head of the local bank) of each Federal reserve bank, shall report to the Federal Reserve Board any undue, unauthorized, or improper use of such credit facilities, together with his recommendation for remedial action in the matter. The Federal Reserve Board may, in its discretion, suspend for not more than one year from the use of the credit facilities of the Federal reserve system any member bank making undue, unauthorized, or improper use of such facilities. Thus the Washington board, not the local Federal reserve bank, is to be policeman to the member banks.

Section 8 provides that the Federal Reserve Board (not the Federal reserve bank) shall have power to fix for any member bank the percentage of its capital and surplus, which may be represented by loans on collateral security, and that the board shall have power to direct any member bank to refrain from increasing its security loans.

15-DAY NOTES AGAIN

Section 11 provides that member banks' borrowings on 15-day notes shall bear a rate 1 per cent higher than the rediscount rate, and that any member bank which, after warning, shall lend money on stocks and bonds or to stock-exchange members, investment houses, or dealers in securities, for the purpose of purchasing or carrying investment securities, except obligation of the United States, shall have its loan called and shall be ineligible as a borrower at the reserve bank on 15-day paper for a period to be determined by the Federal Reserve Board.

NATIONAL BANKS TO UNLOAD BONDS

Section 15 repeals the authority heretofore given national banks to buy and sell marketable obligations for their own account, except as prescribed by the comptroller; but in no event shall the total amount of investment securities of any obligor or maker exceed 10 per cent of the issue, nor shall the total amount of all securities held exceed 15 per cent of the capital stock of the bank and 25 per cent of its surplus. It forbids them absolutely to underwrite the issue of securities. The limitation to 10 per cent of the issue is new. The present limitation is that the total securities of any one obligor shall not exceed 25 per cent of capital and surplus. The limitation on the total holdings of investment securities is also new. These requirements will force national banks to dump their bonds in a period when it is difficult indeed to sell investment securities of even the highest grade to investors, for the bill prohibits banks from holding as well as purchasing for their own account investment securities except as prescribed. This is one of the worst sections. It will gravely depress security prices and so impair the capital and surplus of many banks and trust companies, even though they are not directly subject to the section.

Section 25 amends section 5200 of the Revised Statutes so that subsidiaries' obligations are figured in the amount a national bank may lend to one borrower; and that no obligation of a broker or member of a stock exchange or similar organization, nor of any finance company, securities company, investment trust or similar institution, or of any affiliate shall be subject to the exceptions in favor of bills of exchange, acceptances, etc., provided under section 5200; and that all such obligations shall in every case be subject to the limitation of 10 per cent.

Section 26 also overrules these exceptions to section 5200 with regard to all collateral loans.

Section 18 prohibits banks from acting as correspondents of brokers, leaders, and investment bankers, and vice versa, and prohibits any of the latter from receiving deposits or being directors of national banks and member banks.

PUNISHMENT OF ALL BORROWERS ON COLLATERAL SECURITY

Throughout the bill, the phrase, "loans protected by collateral security," is repeated as the blanket definition of the kind of loans member banks are not to make with Federal reserve credit. Bad as it is to penalize loans on collateral to brokers, securities dealers, investment bankers, etc., it is doubly bad to punish many borrowers on collateral whom there is no intention to punish.

Even if, for the sake of argument, one were to accept the theory that it is sound and proper to penalize and discriminate against call loans on the New York Stock Exchange and those banks that make them, even then it is hard to see how Congress could go so far as to outlaw all stocks and bonds and loans upon them and investments in them. Most people invest their savings in stocks and bonds, and if they borrow on them at all do so for business or domestic needs in these hard times. Must they be punished too so that no wicked speculator shall by chance escape?

INCREASE RESERVE AGAINST TIME DEPOSITS AND REPURCHASE AGREEMENTS

Section 13 requires a gradual increase over five years in the reserves carried against time deposits from 3 to 13 per cent in central reserve cities, to 10 per cent in reserve cities, and 7 per cent in other cities. This clause alone should guarantee for a 5-year period bank failures and deflation.

In clause (d) it prohibits loans "for others." In clauses (f) and (g) it restricts or suspends the sale of reserve balances, and provides that, in computing required reserve balances, the liability created by every repurchase or other similar agreement shall be added to net deposits.

WRITE DOWN REAL ESTATE

Section 14 requires the comptroller at every examination to revalue real estate security for national-bank loans, which under present conditions would probably mean that all the loans secured by real estate are undersecured. It reduces the amount of real-estate loans which a bank may have from 25 to 15 per cent of its capital stock and surplus. It authorizes national banks to invest the amount of their time deposits in real-estate loans and savings bank securities, and members banks must report such investments at market value. It is provided that all the property of any insolvent national bank which is acquired under this section is to be applied by the receiver first to the payment of time deposits. National banks and member banks are required to comply with the terms of this section within two years.

CHAIN BANKS AND AFFILIATES

Section 4 disfranchises chain banks from electing Federal reserve directors. Section 6 requires reports from affiliates.

Section 9 limits member-bank loans to and investment in and loans upon the securities of affiliates to 10 per cent of the capital and surplus of the bank, and under section 25 such loans to national bank affiliates shall also not exceed the affiliate's paid-in capital. All such loans must be secured by 120 per cent listed securities or 100 per cent eligible paper or savings-bank investments.

Section 17 requires national banks to separate the stock certificates of the bank from the stock certificates of the affiliate within two years.

Section 19 amends section 5144 of the Revised Statutes to prohibit anyone but the true owner voting on national-bank stock and prohibits anybody voting more than 10 per cent of the stock of a national bank, except under conditions specified in section 20, requiring an affiliate to make reports and submit to examinations by the comptroller, to hold United States obligations equal to 10 per cent and other assets equal to an additional 15 per cent of the capital stock owned by it in the national bank to cover its stockholders liability, etc.

Section 25 amends section 5200 further so that the aggregate amount of the obligations, including repurchase agreements, of all the affiliates of a national bank shall not exceed 10 per cent of the capital stock of the bank and surplus,

except loans secured by obligations of the United States Government, of the State in which the bank is issued, or a political subdivision of the State, if actually owned by the borrower from the bank. Within three years every national bank affiliate shall be capitalized through the sale of its own stock and not from cash or stock dividends.

Section 27 amends section 5211 of the Revised Statutes by providing for reports of affiliates.

Every national bank affiliate indebted in excess of 5 per cent of the capital and surplus of the parent bank shall publish its portfolio.

Section 28 provides for their examination.

MISCELLANEOUS

Section 7 removes the Secretary of the Treasury from the Federal Reserve Board and removes the Board from the Treasury building.

Section 10 (12 B) provides for a liquidating corporation and section 5 turns over the net earnings of the Federal reserve banks to the liquidating corporation.

Section 21 contains an excellent provision permitting statewide branch banking, and permitting such branch banking beyond State lines in special circumstances.

Section 23 contains an excellent modification of the usury law, affecting national banks.

Section 24 limits the rate of interest which the banks may pay to depositors to one-half the statutory rate, and in the case of interbank deposits to the discount rate of the Federal reserve bank or $2\frac{1}{2}$ per cent which ever shall be smaller.

Section 29 provides for the removal of directors or officers of member banks who have misbehaved.

To summarize, the revised Glass bill is well devised to force further and greater deflation and to prolong and deepen the depression. It would (a) force the liquidation of loans on stocks and bonds and investments in stock and bonds; (b) force the separation of national bank affiliates; (c) impose a rate one per cent above the discount rate on member banks' 15-day notes, and thus contract credit, jeopardize the Government's financing and depress all bonds; (d) force member banks gradually to increase their reserves against time deposits from 3 per cent to 13 per cent in central reserve cities, to 10 in reserve cities, and to 7 per cent in other cities; (e) force member banks to write down their real estate and real-estate loans; (f) prohibits members banks from acting as correspondents for, or making deposits with, bankers, brokers, and others engaged in the business of buying and selling securities; (g) deprive the Federal reserve banks of their autonomy and subordinate them further to the board in Washington and to an open-market committee; (h) destroy the expected good effects of the Glass-Steagall bill.

STATEMENT OF R. M. HANES, REPRESENTING THE WATCHOVIA BANK & TRUST CO., WINSTON-SALEM, N. C.

Mr. HANES. I would like to comment on one or two features of the bill as it affects us in North Carolina.

Mr. Chairman and Senator Glass, we have had in North Carolina a severe upheaval in banking over the past two years. Starting with December, 1930, we lost from 50 to 75 banks, and then, starting with September of last year, up until the 1st of February of this year, we lost something like 100 to 150 banks. We have lost only 2 banks, I believe, since the 1st of February.

We are very anxious in North Carolina, if possible, that nothing be done, no drastic legislation be had at this time to do what we think would probably upset the situation again. It is quiet now. I think the public hysteria is over. Our people are satisfied that the banks that have gone through are good, and we are very anxious that nothing drastic be done, if possible.

Senator GLASS. What caused the failure of the 200 banks?

Mr. HANES. I think public hysteria to a great extent, sir. A great many very good banks, that should be going to-day, closed because of the hysteria. Depositors became frightened, went on to the banks, and asked for their money, and the banks could not liquidate their investment holdings fast enough to pay them.

Senator GLASS. They were largely frozen?

Mr. HANES. Yes, sir; largely frozen.

Senator BROOKHART. Members of the Federal reserve system?

Mr. HANES. No, sir. We only have five State banks left in North Carolina, members of the Federal reserve system.

Senator BROOKHART. Some of the State banks failed?

Mr. HANES. Yes, sir. Some national banks, too.

Senator BROOKHART. Of course, they would be members.

Mr. HANES. Yes.

We think that section 11 of the bill is detrimental, and we would like to see it either modified tremendously or left out. We think a 1 per cent penalty for borrowing on 15-day paper is bad; and we also object to the Federal Reserve Board saying how we shall invest our money. We think that should be left to the discretion of the banker, and we do not believe that legislation is going to make good bankers of poor ones. We also object to the liquidating clause. In the case of the bank I represent, for instance, we would have to put up \$265,000 of our funds to give back to the depositors of the closed banks their funds.

Senator GLASS. What are your deposits?

Mr. HANES. About forty-two or forty-three million dollars, sir.

Senator GLASS. How do you figure the \$265,000?

Mr. HANES. As I understand the bill, it is one-half of 1 per cent.

Senator GLASS. One-fourth of 1 per cent is the first call. The total is one-half of 1 per cent.

Mr. HANES. Yes; but I understand one-half of 1 per cent is the amount we would be liable for if called on.

Senator GLASS. You anticipate there would be more than one call?

Mr. HANES. A lot of these things we have not anticipated, Senator, in the past two years that have come on us.

Senator GLASS. Has the full capitalization of the Federal reserve banks which have been in existence nearly 19 years been called?

Mr. HANES. No, sir; I do not think so.

The CHAIRMAN. Would you have a different attitude toward that if it were deferred a little longer?

Mr. HANES. No, sir; I do not think we would.

The CHAIRMAN. Do you think there is any need?

Mr. HANES. I do not think private funds and stockholders' funds should be put up to help banks in distress. We do not think that is fair or right. We do not think we have a right to take our stockholders' funds and prejudice their rights for other stockholders or other depositors.

Senator GLASS. Did you subscribe to the capital of the National Credit Corporation?

Mr. HANES. Yes, sir.

Senator GLASS. That was 2 per cent, was it not?

Mr. HANES. Yes, sir.

Senator GLASS. Do you think it was all right to subscribe your depositors' money to that and all wrong to subscribe it to this?

Mr. HANES. Yes, sir; because that was the thing we had direct control of or part of the control of and did it purely as an emergency measure. It was not done to be strung out over a period of years. Our directors felt the same way about that. It was a question of self-protection to them in a case of emergency.

Senator GLASS. Is not this a question of protection, and is it not a profitable investment?

Mr. HANES. I think the difference, sir, is we were protecting our banks in North Carolina and not banks all over the United States, to a great extent, and we were more intimately connected with them.

Senator GLASS. How many member banks failed?

Mr. HANES. I do not know the exact number, sir. There are only five now.

Senator GLASS. Do you not think the depositors of those member banks would like to get what is coming to them rather than to wait over an extended period of years to have it doled out to them by a receiver?

Mr. HANES. Yes; I think they would.

Senator GLASS. That is what this bill provides.

Mr. HANES. It is only a question of whether the stockholders of our banks should give up their funds to help the depositors of another bank. We do not think that it quite fair.

Senator FLETCHER. The run on the one bank and the failure of that one had a bad effect on all the banks, did it not?

Mr. HANES. Yes, sir. It multiplied the intensity of the trouble, of course.

Senator FLETCHER. So if you can prevent a bank from failing it helps the whole system, helps the confidence of the depositors in the whole system. In other words, there ought to be a little spirit of cooperation between banks.

Mr. HANES. Yes, sir. I think that is quite true, sir. I think that has been shown by the National Credit Corporation. The cooperation they brought about did a tremendous good.

Senator GLASS. Why would not this do a tremendous good?

Mr. HANES. I think it probably would, sir, if it was wisely handled and properly handled.

Senator GLASS. If it was wisely handled it was the thought of the committee it would show a profit on your investment. You would get 30 per cent of the earnings of the corporation.

Mr. HANES. Of course, it depends on the management altogether, as to whether there is going to be any 30 per cent.

Senator GLASS. It depends upon the management of the National Credit Corporation whether there would be any per cent, too.

Mr. HANES. Yes, sir. But I tried to make it clear that that was a purely emergency thing, where the bankers were largely interested and their full time was put in in seeing that it was properly managed. I do not believe that that would be possible with a corporation that is run over a period of years.

Senator FLETCHER. The Federal Reserve Board passed a substitute for your section 11. Have you seen their substitute and examined it to see whether that would be satisfactory?

Mr. HANES. Yes, sir; I just looked at it hurriedly this morning.

Senator GLASS. You think it is all right, then, to take the taxpayers' money and secure the deposits of failed banks? That you think is all right?

Mr. HANES. I think it much fairer, sir, than taking the well-managed funds of stockholders to pay losses of badly-managed banks with. Bank solvency is a question of public good. The public as a whole are depositors in banks.

Senator GLASS. The taxpayers do not derive any profit from the operation of this proposed liquidating corporation. That is a liquidating corporation proposed by the Federal Reserve Board. Why should I, as a taxpayer, be taxed to do this thing when I have no interest in it?

Mr. HANES. You have the interest, sir, as a depositor in some bank.

Senator GLASS. How do you know?

The CHAIRMAN. It is a very small part of the population that are depositors, is it not?

Mr. HANES. Certainly a larger percentage are depositors than are stockholders. I am not proposing to take the taxpayers' money. I am simply saying—

The CHAIRMAN. If we talk about taking the taxpayers' money for the protection of depositors, we get a very involved question.

Mr. HANES. I do not know, sir. We are taking it for a lot of purposes.

Senator BROOKHART. If you are taking the taxpayers' money to substitute for this National Credit Corporation or Reconstruction Finance Corporation, I guess it finally comes back to the taxpayer, does it not?

Mr. HANES. Yes, sir; I should think so.

Senator GLASS. As I concede, we have taken the taxpayers' money for a good many purposes.

The CHAIRMAN. We have been taking it to help the big banks, have we not?

Senator GLASS. We took \$40,000,000 of it to help one bank.

Senator FLETCHER. You mention section 11. What other section do you wish to criticize?

The CHAIRMAN. We took that in the hope of preventing a disaster.

Mr. HANES. They were the two principal sections that we objected to. The other is section 12 B.

Senator GLASS. If we should eliminate the 1 per cent penalty, what would be the objection to the section?

Mr. HANES. I think the objection still holds, sir, that the Federal Reserve Board would say to us how much of our funds we could put in security loans, which we object to. We think we can handle that ourselves better than they can tell us to. I hope so.

Senator GLASS. Have they not that authority now?

Mr. HANES. It is not as definitely prescribed as it is in here, as I understand it. This makes it obligatory upon them. I do not think it is now.

Senator GLASS. They have, under that provision of existing law, unlimited authority to make any assessment against 15-day paper they please, have they not?

Mr. HANES. Yes, sir.

Senator GLASS. So when it comes to be a question of authority, this is a restriction of authority rather than an expansion?

Mr. HANES. I think this makes it obligatory to say to a bank, "You shall carry only so much in security loans," as I understand the bill, sir.

Senator GLASS. No. It simply authorizes the board to say that if a bank is jeopardizing its business and depriving agricultural, commercial, and industrial enterprise of its opportunity to get credit on reasonable terms, it shall not extend that character of loans.

Mr. HANES. Yes, sir.

Senator GLASS. It does not say it shall not make them.

Mr. HANES. I think that would have the effect, sir, of this, as I read the law and as the Federal reserve law now exists: We can loan any amount of money on open paper, that is, one-name or two-name or three-name paper. We might have some one come in who would want to borrow ten, fifteen, or twenty-five thousand dollars who would offer perfectly good and liquid collateral. We would say, "No, we are prohibited from taking that, but we will take your open note and the money will go to the same cause."

Senator GLASS. You will not be prohibited from taking it unless, upon examination, the Federal reserve bank at Richmond reaches the conclusion that your extension on speculative loans is so great as to jeopardize the business of your bank or to deprive legitimate commerce of accommodation.

Mr. HANES. That is just the question, sir; whether these loans are speculative or not. They are loans on security, but a great many of them go right into commerce and industry.

Senator GLASS. That would be determined by the board of directors of the Federal reserve bank.

Mr. HANES. It is a very hard thing to determine, sir.

The CHAIRMAN. Whether they would probably be slow or active.

Senator GLASS. Unhappily there is no imperative reason to suppose that the Federal reserve bank would ever do that. It is permitted to exercise the authority it already has, and it has unlimited authority to fix the rate of interest on 15-day loans and never has done it.

Mr. HANES. Yes.

Senator FLETCHER. I did not quite catch whether you approved of the Federal Reserve Board's substitute for that section 11 or not.

Mr. HANES. Well, as I read it very hurriedly this morning, I think the Federal reserve substitute leaves the law just as it is on 15-day loans.

Senator GLASS. I know, but they covered that whole proposition in section 3. Do you approve of their section 3?

Mr. HANES. I do not know what their section 3 is. I read it just this morning in the paper and very hurriedly. I have not had opportunity to study it at all.

Senator GLASS. Their section 3 gives unrestrained, unlimited power to the Federal Reserve Board to fix a percentage of loans, not only on speculative paper but on real estate and on commodity paper. Do you approve of that?

Mr. HANES. I do not think the Federal Reserve Board has ever abused its power so far, and I do not think it would in the future.

Senator GLASS. Why do you think it would as to section 11?

Mr. HANES. I think section 11 is very specific and very definite but almost obligatory on them.

Senator GLASS. Oh, no. It leaves it entirely in their discretion. In other words, under that section the national bank, for example, may loan \$50,000,000 on speculative security or \$100,000,000, for that matter, but only after it has extended loans on paper of that character.

Mr. HANES. What borrowing we can do we do not do on eligible paper. We borrow on Government securities altogether, because it is much easier to go to the Federal reserve bank and get money for two or three days by simply sending a note in and use it. Otherwise we would have to go through the files, get out the eligible paper and have it all worked up into proper sheets and sent to Richmond and then have it sent back to us as it matures. It is quite a lot of trouble to do that.

Senator GLASS. Suppose there were no Government bonds. What would you do?

Mr. HANES. Then we would have to do just what we could do. If there were no Government bonds we would have to buy other securities.

Senator GLASS. When that provision was inserted in the Act there were no Government bonds available for 15-day loans in appreciable amounts.

Mr. HANES. There are a lot available now.

Senator GLASS. When we drafted the law there were none available. We never would have authorized the use of them, because the Federal reserve system is a commercial system; it is not an investment banking system; and so far from being a speculative banking system that we very definitely precluded speculative paper from the eligibility clause of the bill.

Mr. HANES. Yes.

Senator MORRISON. Were you through, Senator?

Senator GLASS. Yes.

Senator MORRISON. I noticed in your reference to section 3 a while ago you did not seem to think it was as mandatory as section 11. I want to call your attention to line 18 on page 8, section 3, where it says:

Such facilities shall not be extended to member banks for the purpose of making or carrying loans covering investments or facilitating the carrying of or trading in stocks, bonds, or other investment securities other than obligations of the Government of the United States.

Do you not think that is pretty mandatory?

Mr. HANES. Yes, sir; I think it is.

Senator MORRISON. Do you understand that to be the law now?

Mr. HANES. No, sir; I do not.

Senator GLASS. What do you understand by this?

Mr. HANES. I understand the law, as it is now, is permissive entirely; but this, as I read it, is obligatory.

Senator GLASS. The law, as it exists, is absolutely negative. It says that the Federal Reserve Board, in its definition of eligible paper shall not include notes, drafts, or bills covering investments.

Mr. HANES. That is simply the rediscount privilege. That does not say you can not hold these in your portfolio and still rediscount. This bill does, as I understand it.

Senator GLASS. No; not what has been read there, does it? What has been read there says that—

The Federal reserve bank shall not permit its facilities to be used for purchasing or carrying or trading in investment securities or notes, drafts, or bills issued or drawn for the purpose of carrying or trading in stocks, bonds—

And so forth.

Mr. HANES. Yes..

Senator GLASS. Is not that the exact language of section 3 as we have it in the bill?

Mr. HANES. It is, sir; but, as I know the Federal reserve act now, that simply applies to rediscounting. That does not say you shall not carry that in your own portfolio if you want to.

Senator GLASS. Neither does the section that Senator Morrison has read.

Senator MORRISON. Senator Glass, right there, that is a very important matter to me. I thought it did, and I interpreted it that way. If I am wrong I would like to be convinced of it.

Senator GLASS. It applies to the Federal reserve bank, not the member bank. It does not forbid the member bank to extend its facilities for investment.

Senator MORRISON. The objection I see, as I read it, is they may pass regulations regulating their member bank.

Senator GLASS. No; regulating the Federal reserve bank; that the facilities of the Federal reserve bank, its rediscount facilities, shall not be used for that purpose.

Senator MORRISON. For a bank that it has made rules governing, and if it breaks them it may punish them by not letting them have any accommodations for 12 months.

Senator GLASS. No.

Senator MORRISON. I can talk to you privately. That is my chief objection.

Senator GLASS. I think I can point out to you privately, as I could publicly, that that is not the meaning of it at all.

Senator MORRISON. That is the way it reads to a country lawyer like me.

Senator GLASS. That is simply a transfer of the text of the existing provision of law to that section of the bill, with the proposed amendment by the Federal Reserve Board. It is just commending itself to the bankers and enlarges the power of the Federal Reserve Board in that respect.

Senator MORRISON. It goes on to say:

Only if such discounts, advances, and accommodations are intended for the accommodation of commerce, industry, and agriculture, and the Federal Reserve Board may prescribe regulations further defining and regulating the use of the credit facilities of the Federal reserve system.

Senator GLASS. Of the Federal reserve bank, not of the member bank.

Senator MORRISON. Yes; but the member bank, of course, gets it from the Federal reserve bank.

Senator GLASS. Yes; but the existing law, Senator, for 19 years has made that provision.

Senator MORRISON. When they ask for the discount it must be for that purpose, and with that I heartily agree with you as much as anybody.

Senator GLASS. That is all there is to it.

Senator MORRISON. When it comes to their saying, "But I won't discount it for you because you have got too much of your securities in other things——"

Senator GLASS. It does not say that.

Senator MORRISON. That will get rid of a heap of trouble.

Mr. HANES. Section 11, page 25, does say that, does it not, Senator?

Senator MORRISON. That is with reference to the 15-day loans.

Senator GLASS. Section 11 with respect to that authorizes the Federal Reserve Board, if it conceives a bank has overextended in speculative transactions, to warn it not to further extend its loans, and if it should disobey the warning, it may be suspended. That is covered in the proposed amendment to section 3 of the bill recommended unanimously by the Federal Reserve Board.

The CHAIRMAN. Do you not think the danger of trouble from that source is pretty remote?

Senator MORRISON. I think they have been doing it morally, like that witness said this morning. I know they have been in my section of the country trying to regulate them all the time.

Senator GLASS. In other words, they made a mighty feeble attempt.

Senator MORRISON. They wrecked a great many people by it.

Senator GLASS. And that provision of the bill was inspired by a notable episode. The Federal Reserve Board here at Washington undertook, under its authority as expressed in the act, to mildly remonstrate with a speculative bank, a tremendously speculative bank in New York, against the extension of its loans for stock gambling purposes. That is the plain fact. That speculative bank, as I have said, figuratively told the Federal Reserve Board to go to hell; it was going to do as it pleased in the matter, and that it was going to the very next day rediscount to the extent of \$25,000,000 and loan it on the market. The president of that bank, who was also a director, a sworn officer, of the Federal reserve system, took the position that his obligation was to the stock market rather than to the Federal reserve bank. Now, that provision is simply intended to say that if a thing of that sort should occur again, that bank could be suspended from the use of the Federal reserve facilities.

Senator MORRISON. Senator, I think that is the intention. But at the same time, in great sincerity, I think it goes to the extent of giving them the power to undertake directly, and it is made mandatory, to control and regulate all of their investments; and I do not think they ought to have it.

As to the evil that you are striking at there—this is all aside—I have a profound sympathy with your view. May I ask you this, Mr. Haines, I do not want to ask you if you mind telling, there may be some business reason why you would not like to tell, but may I ask what percentage of your loans are now eligible for discount?

Mr. HANES. About 15 per cent, sir. We have about \$3,500,000 of eligible paper.

Senator GLASS. And generally speaking, as a business practice, the percentage of eligible paper in our section of the best banks as related to the whole sum of their credits is small, is it not?

Mr. HANES. Yes, very small.

Senator GLASS. Has the Federal reserve bank, as you understand it, any legal power now to dictate to you except in a moral way what you shall invest in so far as your bank is concerned?

Mr. HANES. I think they probably have under the act as it is now if they should want to do it, but it never has been customary. I do not think they could go as far as they could under this act at all.

Senator GLASS. According to my interpretation of it, it is made mandatory, is it not?

Mr. HANES. That is the way I read it, sir.

Senator GLASS. They shall do it under the above sections. You would not want to see that done, would you?

Mr. HANES. No, sir; I would rather not.

Senator GLASS. Well, would it not endanger the whole fabric of our business life to have to restrict those credits and collect them and reinvest them, at this time especially?

Mr. HANES. Yes, sir; I think it would.

Senator FLETCHER. You did not point out what objection to section 12B you had. You said you objected to it.

Mr. HANES. That is the liquidating corporation provision.

Senator FLETCHER. You object to that whole plan?

Mr. HANES. Yes, sir.

The CHAIRMAN. I thank you very much.

(Whereupon, at 1.10 o'clock p. m., a recess was taken until 2.30 o'clock p. m.)

AFTERNOON SESSION

Pursuant to the expiration of the recess, the committee reconvened in the Interstate Commerce Committee room in the Capitol at 2.30 o'clock p. m.

The CHAIRMAN. The committee will come to order. The first witness is Mr. Burgess. He wanted to appear for a few minutes.

STATEMENT OF W. RANDOLPH BURGESS, DEPUTY GOVERNOR OF THE FEDERAL RESERVE BANK IN NEW YORK CITY

The CHAIRMAN. You may take a seat, Mr. Burgess, and give your full name and address and your business connections and whom you represent.

Mr. BURGESS. W. Randolph Burgess, deputy governor of the Federal reserve bank in New York, New York City.

Mr. Chairman, I am appearing in behalf of Governor Harrison. Governor Harrison was scheduled to appear before this committee this afternoon at 2.30. Unfortunately, his brother lies very critically ill, and I am afraid at the point of death, and so he is not going to be able to be here and asked me to come and express to you

personally his regrets and not being able to fulfill his appointment and to ask if there is any possible way in which the committee could arrange to hear him at a later time. I realize the difficulties in that. The New York bank, of course, is very closely concerned with the substance of this bill; our directors are most anxious that Governor Harrison should be heard, and if there is any convenient way in which that could be arranged, he and they would certainly appreciate it.

Senator WALCOTT. Mr. Chairman, may I suggest that we ask Doctor Burgess if it would not be just as convenient for Mr. Harrison, and equally good for us, if he submitted written comments as part of the record, rather than to extend our hearings?

The CHAIRMAN. The Chair suggests that after hearings are closed we go into executive session and take up those matters. I am glad to have your explanation.

Senator GLASS. I would like to go upon the record here, in order that it may not appear that Governor Harrison has no opportunity to comment upon the provisions of this bill, that Governor Harrison has complete knowledge of, I might say, every provision of the bill except one, and has had for three weeks.

I want to say, furthermore, that I personally called Governor Harrison on the phone, as members of the subcommittee will recall, by direction of the subcommittee.

The CHAIRMAN. Some time ago?

Senator GLASS. Yes, sir.

The CHAIRMAN. A month or more ago?

Senator WALCOTT. About two weeks ago.

Senator GLASS. And said to him that the committee would give him public hearing if he desired it, and he very explicitly, I may say emphatically, stated that he did not want to be heard. I say that, Mr. Burgess, in order that the impression may not get abroad that we have done anything in a corner and have not given everybody an opportunity to be heard.

The CHAIRMAN. Go ahead and make any further statement you want.

Mr. BURGESS. Mr. Chairman, I must just say that Governor Harrison reported the conversation to me and I think his understanding of it was that he did not care whether the hearing would be public or private, but his negative response was to the question of whether he desired a public hearing; that he did, however, desire a private hearing, a hearing of some kind, whether public or private.

Senator GLASS. Well, of course, you know we gave Governor Harrison repeated frequent private hearings.

Senator COUZENS. Mr. Chairman, I move that Governor Harrison be permitted to file a statement with the committee.

Senator GLASS. I can see no objection in the world to that.

The CHAIRMAN. If there are no objections, the matter will be disposed of now in that way and he will be given permission to file a written statement.

LETTER OF GEORGE L. HARRISON, GOVERNOR FEDERAL RESERVE BANK OF NEW YORK

FEDERAL RESERVE BANK OF NEW YORK,
April 7, 1932.

The attached letter of Governor Harrison, dated April 7, has been read and unanimously approved by the directors of the Federal Reserve Bank of New York present at their meeting on April 7, 1932.

J. HERBERT CASE, D. C. WARNER,
THEO. F. WHITMARSH, OWEN D.
YOUNG, ALBERT H. WIGGIN, C. M.
WOOLLEY, W. H. WOODIN, SAM'L
W. REYBURN.

FEDERAL RESERVE BANK OF NEW YORK,
April 7, 1932.

HON. PETER NORBECK,

*Chairman Committee on Banking and Currency,
United States Senate, Washington, D. C.*

DEAR MR. SENATOR: I am sorry that my brother's death prevented me from appearing personally before your committee on Tuesday, March 20, the day on which an opportunity was given to me to express my views with respect to the provisions of Senate bill 4115 now before your committee. However, I very much appreciate the action of the committee in giving me this opportunity to present to it a memorandum of our views with respect to this important bill.

Of course, it would be the wish of the committee and of all connected with the Federal reserve system, to do everything properly within our power to accomplish two objects: First, to check the present depression in business and trade, and second, to prepare the means for avoiding, as far as may be possible to do so by legislative or administrative action, a repetition of conditions which may have contributed to the depression. We all have the same interest and the same objectives. The task before us, however, is how to devise the means of accomplishing these two purposes.

It is our opinion that Senate bill 4115 is directed more toward the second objective, that is, a control of possible future inflation or abuses of credit, than it is toward the first and at the moment the more important objective, that is, a restoration of more normal business conditions. Apart from the relatively few provisions in the bill, such as those relating to branch banking and possibly the liquidating corporation, the great majority of its substantial sections appear to us to be deflationary or restrictive in their effect. To the extent that the pending bill endeavors at this time to prevent possible future excesses, it would operate as a restraint upon, and would probably require a drastic readjustment of, the banking and investment machinery of the country. This would be a deterrent, both actual and psychological, to the recovery from the present depression, which is one of the most severe in our history. That depression affects all classes of production, industry, agriculture, and trade. It has been accompanied by an extremely rapid deflation in commodity prices and in the general price level. It has resulted in unemployment never before exceeded in our history. It has been accompanied by receiverships and defaults, and in the closing of many banks throughout the country. As time goes on prices, wages, and incomes are being reduced and unemployment is not decreasing.

Regardless of the causes, we are now confronted with an economic crisis which is the immediate and prime concern of every one of us.

With these conditions in mind, our views with respect to the proposed legislation may, for the purposes of this discussion, be summarized by the following general statement of principles which we believe to be important:

First. The bill, through many of its provisions, tends further to centralize in the Federal Reserve Board the control of operations of the Federal Reserve banks and the member banks. We believe in the basic principle of the Federal reserve act that the public interest will best be served by leaving to the boards of directors of the several Federal reserve banks autonomous powers of operation within the terms of the law, and by leaving to the Federal Reserve Board general and broad powers of supervision as was always contemplated by the framers of the Federal reserve act. All the more important is it, in our judg-

ment, that the operations of the member banks within the terms of the law should be left to the management of the respective boards of directors.

Second. The Federal reserve banks, as any bank of issue, should endeavor to control unnecessary expansion or excessive uses of credit by the use of the discount rate, supplemented by appropriate open-market operations, rather than by arbitrary or dictatorial "direct action." It is not possible, nor would we deem it wise if possible, for the Federal reserve banks or the Federal Reserve Board or any one group of persons to control the uses to which the credit of the country shall be put once it is let loose. It is one thing for Federal reserve banks, through the discount rate and through open-market operations, to influence the total volume and the price of credit. It is a very different and, we believe, an unwise thing for the Federal reserve banks or the Federal Reserve Board, through so-called "direct action," to attempt to control or dictate the loan or investment policies of many individual banking institutions of the country.

Third. The danger of speculative excesses is not necessarily inherent in granting bank loans based upon collateral security, or in investing bank funds in capital securities. A large proportion of bank credit in the United States has always been based upon the obligations of or equities in American industry or business institutions. That is a necessary means of extending credit to many classes of legitimate borrowers whose other credit alone is not adequate to support a bank loan.

These are our general observations with regard to certain broad questions of principle raised by the proposed bill. It is difficult in the space of a letter to offer detailed comments as to specific provisions of the bill. There are, however, certain general comments which we think should be made with reference to some provisions of the bill which involves some of the points outlined above.

The first, and perhaps the most important, question arising now in connection with this bill is the question of timeliness. Just as in time of war, the interests and the energies of this country are now concentrated on the single problem of recovery from depression, of restoring work to several million unemployed, of raising commodity prices to a point where debtors may meet their debts, of removing want, distress, and fear. A beginning has been made in curing the basic causes of the depression, in reducing bank failures, in restoring confidence, and in making credit more freely available. It would be most unfortunate should anything now be done to interfere with or retard the forces of recovery. We trust, therefore, that in its consideration of the pending bill the committee will give most careful consideration to the probable effects on public sentiment and the credit situation which may arise from its action on this bill. A threat of credit restriction or dislocation of the financial machinery may at this time prove a seriously disturbing factor.

Even were it not for the present critical situation it must be recognized that a fundamental revision of the banking law, going to the very roots of the principles of central banking, is necessarily a large undertaking, and one which should only be carried through on the basis of a considerable consensus of opinion as to the major features. While the Senate committee has been working for more than a year, the definite proposals in the present bill have been before the country only a limited number of weeks, at a time when men's minds have been largely diverted to other matters and when men's emotions are greatly stirred. It is doubtful whether legislation of this sort should ever be hurried unless there is some pressing public need for it. The evidence before your committee tends to indicate that there is no such need just now. On the contrary might not haste be particularly unfortunate at a time like the present?

As indicated in our preliminary summary, it seems to us that the pending bill is based upon questionable principles in at least three particulars.

First, one basic principle of the Federal reserve system is that the system should constitute a democracy of credit with a large measure of local autonomy. As we interpret many of its provisions the question arises in our minds whether the bill might not do much to defeat this fundamental principle. It would increase to a great extent the powers of a Government board, not only over the Federal reserve banks but over the member banks as well, and it would give this board no small measure of responsibility for the management and policies of individual banks.

Second, the bill proposes to check speculation by increasing Federal reserve powers of restriction and prohibition upon the operations of individual banks. This is the method of "direct action" which has its uses as a method for

dealing with individual banks which may be using more than their share of Federal reserve credit, but it is not an effective or suitable method for general control of credit or the uses to which credit will be put. The proper and most effective instruments of credit policy are open-market operations and discount rates, and the influence exerted by a reserve bank on the loan and investment policy of individual member banks ordinarily has but limited effect on credit conditions as a whole. Not only is the type of "direct action" which this bill embodies in law usually ineffective as an influence on general credit conditions, but it involves the assumption by the Federal reserve system of a responsibility for the management of individual member banks which could not effectively be fulfilled. For proper and effective control of credit conditions the traditional methods of influencing the volume and cost of credit by the discount rate and open-market operations must be relied upon. The proposals in sections 3, 8, and 11, of the bill before you would, we believe, prove both ineffective and seriously embarrassing and detrimental to the Federal reserve system and the member banks.

Third, the bill attempts in considerable measure to divorce the banking system from the capital market, and would do much to disturb the mechanism of the capital market, the free functioning of which is now so important to a recovery from existing business conditions.

There are really two banking systems in the United States, the organized system of incorporated banks under State and National charter, and in addition an unincorporated, less organized system, generally known as the capital market. This second banking system, this capital market, is the channel through which the investors of this country place in the hands of American business each year two or three times as much money as is placed through the incorporated banks.

Business in the United States is even more dependent upon this capital market than upon the banks. Without the capital market new enterprises would be curtailed, old businesses would be kept from expansion. The capital market is particularly important at times like the present when business is struggling to revive from depression. The almost complete lack of issues of new securities in recent months has been an important cause of depression, and the gradual revival of new issues will be one of the first signs of business recovery.

Admitting certain past defects and the need for the prevention of possible future abuses of the capital market, we believe that any material disorganization of that market would now be most unfortunate.

At a number of points these two banking systems are related. The banks participate in one way or another in the origination and distribution of new issues. A substantial part of the securities sold in the United States is sold through banks. Banks themselves are large buyers of bonds. The bill before this committee proposes in some measure to disturb these relationships, and at many points provides for a divorce of the banking system and the capital market.

The broad question to be determined is the extent to which the capital market should be divorced from the banking system and removed from all supervision, or whether its relations with the banking system should be maintained and placed under appropriate supervision. It is an involved and difficult problem, but the divorce proposed in this bill appears to be certainly unwise at the present time when business recovery is so dependent on the proper functioning of the capital market. As a permanent matter the capital market is necessarily dependent on the banks for aid in the intermediate stage between the origination and distribution of an issue and for entirely proper credit to legitimate borrowers offering securities as collateral.

Your committee has before it a most comprehensive and illuminating report upon Senate bill 4115 presented to you with the unanimous concurrence of the Federal Reserve Board. This report reviews the bill section by section and suggests many changes designed to bring the bill into conformity with sound banking principles. We are in substantial agreement with many of those recommendations, especially in so far as they are purposed to eliminate certain deflationary or restrictive aspects of the bill. But we regret that we must differ with some features of the board's report which we feel still leave the bill open to certain fundamental objections of principle discussed above. Section 3 of the bill even as amended by the Federal Reserve Board gives the Federal reserve system and particularly the Federal Reserve Board extensive and direct powers over the operations of individual member banks.

Section 12 even as amended by the board prescribes detailed rules of operation in foreign transactions, almost sure to prove unnecessary obstacles to the proper handling of those operations. Sections 17 and 18 as amended by the Board go further in a tentative suggestion of divorcing the banks and the capital market than we should think wise at the moment.

In conclusion, there do not appear to us to be any parts of the bill for which there is imperative need for immediate passage, although two sections of the bill are, indeed, of a character which might be expected to be helpful in the present emergency. They are the proposal for a liquidating corporation, section 10 (B), and the proposal for a wider extension of branch banking, section 21. If the liquidating corporation is to prove helpful, however, it would seem to us to be essential that the amendment suggested by the Federal Reserve Board be adopted, since a number of features of the proposal in the pending bill might well be unnecessarily disturbing. The branch-bank proposal would be helpful and useful in providing a mechanism for reorganizing and revitalizing many small banks not now able to render adequate banking service in their communities.

As I stated when I appeared before your committee in January, 1931, and as I reiterated to Senator Glass, chairman of the subcommittee of the Senate Committee on Banking and Currency, in my letter of February 6, 1932—a copy of which I would like to attach—much of the banking trouble which we have experienced in the past has been due not so much to violations of law as to mismanagement within or abuse of the privileges afforded by the law. Competition between the State and National Governments in the granting of charters and in the liberalization of the banking laws has gone further and further to make these legalized abuses possible. Limitations and restrictions in the law intended as safeguards against bad banking are too often regarded as invitations to unwise banking within the law. We fear that no matter how well a law may be conceived and drafted, that danger will always be present unless the management of individual banks is of the highest type. If, therefore, it is not possible at this time, either for practical or political reasons, to provide for one banking system which would include all commercial banks, as we would favor, then it seems to us that one of the most important contributions that may be made to the banking situation would be the adoption of such amendments to the law as might insure better and better management of individual banks, and not the centralization of managerial or dictatorial powers in the Federal reserve banks or the Federal Reserve Board. No law, however perfect in itself, can serve as a substitute for management of individual institutions, and with a dual competitive banking system legislative restrictions often prove inoperative in any event. If too strict in one system, banks shift to the other. If too lenient because of the competition for membership, they sanction bad banking. Ultimately, therefore, the protection of bank creditors and the community must depend largely upon the character and experience of bank management.

Many of the views which we have expressed in this letter as to various questions of principle are but a recapitulation of more detailed views which we have already presented to your committee under date of February 25, 1931, in response to the questionnaire which your committee submitted to all Federal reserve banks.

In case the committee may be interested, I am glad to inclose a memorandum which contains very brief comments regarding each individual section of Senate bill 4115 and the Federal Reserve Board's suggested amendments thereto.

Very truly yours,

GEORGE L. HARRISON, *Governor.*

SECTION BY SECTION COMMENT OF SENATE BILL 4115

Section 2. Definitions—goes with section on affiliates:

We agree with board amendments.

Section 3. Defining conditions of discounts:

We are not in agreement with either the bill or the board's amendment, believing that the powers thereby given to the reserve banks and the Reserve Board would be ineffective to accomplish the implied purpose and would involve responsibilities for the management and operation of individual banks which it would be impossible for the reserve banks or the Reserve Board to fulfill and

the assumption of which would be harmful to the reserve system as a whole and to the individual member banks.

Section 4. Denying votes at reserve bank elections to group and chain banks:

We agree with the board's recommendation. Undesirable at any time.

Section 5. Disposition of reserve bank earnings—goes with liquidating corporation:

We agree with board's amendment.

Section 6. Reports and examination of State member bank affiliates:

We agree with board's amendment. Desirable at some time, in amended form suggested by board, but not necessary now.

Section 7. Changes in Reserve Board composition and terms:

We agree with board's amendment. Desirable some time, in amended form suggested by board, but not necessary now.

Section 8. Limiting collateral loans:

We agree with board's recommendation. Undesirable at any time and disturbing now.

Section 9. Limiting loans to affiliates:

In substance we agree with board's amendment. Desirable at some time, not necessary now.

Section 10. Open market operations:

We agree with board's amendment. No objection to adoption some time, in amended form suggested by board, but not necessary now.

Section 10. Liquidating corporation:

We agree with board's amendment. Prompt enactment might be helpful.

Section 11. Rate and control of borrowing on 15-day advances:

We agree with board's recommendation that this section of bill be eliminated. Undesirable at any time, disturbing now.

We favor board's suggested substitute about maturity of advances—desirable some time, but not necessary now.

Section 12. Supervision of foreign operations:

We disagree with the board's amendment, which prescribes a procedure which is unnecessarily cumbersome and in some respects unworkable. We believe the development of this procedure could more wisely be left to experience.

Section 13. Reserve requirements:

The proposal involves a wholly new method for computing reserves making considerable changes for individual banks. Time should be given for a more general understanding of the proposal with further study as to its effect on individual accounts and institutions.

Section 14. Control of real-estate loans, etc.:

We agree with board's recommendation—undesirable at any time and disturbing now.

We favor board's suggested substitute limiting the cost of bank buildings. Desirable some time, in amended form suggested by board, but not necessary now.

Section 15. Limiting bank investments and security operations:

We agree with board's recommendation. This particular proposal undesirable at any time and disturbing now—though some legislation on this subject warrants later consideration.

Section 16. Increasing capital of new national banks:

We prefer the proposal in the bill to the board's amendment—desirable some time but not necessary now.

Section 17. Stock units and separation of bank and affiliate stock:

We agree with board's recommendation on first half but favor omitting the entire section as likely to be disturbing now. The proposal to separate bank and affiliate stock may wisely be considered later though its desirability at any time is doubtful.

Section 18. Divorce of affiliates:

We agree with board's recommendations opposing section 18 of the bill. Undesirable at any time. The board's tentative substitute we believe would be seriously disturbing now, but might wisely be considered at a later time, though its desirability at any time is doubtful.

Sections 19-20. Supervision of holding companies:

We agree with board's amendments. Desirable some time, in amended form suggested by board, but not necessary now.

Section 21. Branch banking:

We agree with board's amendments. Prompt enactment might prove helpful.

Section 22. Verbal changes caused by 21:

Section 23. Extends limit on interest rates on loans:

We agree with board's amendment. Desirable some time in amended form suggested by board, but not necessary now.

Section 24. Limits interest rates on deposits:

We agree with board's recommendation. Undesirable as long as we have a dual banking system--would be disturbing now.

Section 25. Limits national-bank loans:

We agree with board's recommendation. Undesirable and disturbing.

Section 26. Repeals exceptions to section 5200:

We agree with board's recommendation. Undesirable and disturbing.

Section 27. Reports of national-bank affiliates:

We agree with board's amendment. Desirable some time, in amended form suggested by board, but not necessary now.

Section 28. Examination of national-bank affiliates:

We agree with board's amendment. Desirable some time, in amended form suggested by board, but not necessary now.

Section 29. Removal of officers and directors:

We agree with board's amendment. Desirable some time, in amended form suggested by board, but not necessary now.

FEDERAL RESERVE BANK OF NEW YORK,
February 6, 1932.

HON. CARTER GLASS,

United States Senate, Washington, D. C.

MY DEAR MR. SENATOR: A week ago Tuesday, when I was in your office, you or some of the members of your committee were good enough to suggest that I send to you my comments and suggestions regarding the provisions of Senate bill 3215. I said that I would try to have those comments before you by the following Monday. In the meantime, however, that is, on the intervening Thursday, I was informed of a change in the procedure, to which I understood you and Senator Walcott had agreed, that is, that you and he reconsider the provisions of your bill with Doctor Goldenweiser, of the Federal Reserve Board, and Mr. Burgess, of this bank. In view of this new set-up and the fact that Doctor Goldenweiser and Mr. Burgess were to submit their comments and suggestions as independent experts, I felt, and Senator Walcott agreed, that it would be premature for me to write your committee regarding the provisions of the original bill, since this new procedure would no doubt result in modifications in the published draft in any event.

I now understand that Doctor Goldenweiser and Mr. Burgess are to submit a report to you early next week, and while I do not now want to make any specific comments or suggestions regarding the original draft of the bill, I hope it will not be inappropriate for me to make a few general observations.

During the past two years we have suffered one of the most severe depressions in history. There is no need in this letter to enlarge upon our difficulties. Suffice it to say that production, manufacture, and trade have suffered severely. The general price level has declined approximately 23 per cent; wholesale prices 32 per cent; wage rates perhaps 10 per cent; and weekly income of wage earners about 20 per cent. Unemployment is greater than ever before in history.

Coincident with these things, and partly because of them, we have experienced a wave of bank failures that has caused great distress and alarm throughout the country; over 2,000 of them, or approximately 10 per cent. in the last year alone. Bank credit has declined over \$6,000,000,000 in two years; \$4,000,000,000 in the year 1931; and over \$2,000,000,000 in the last quarter of 1931 alone. The rate of decline has not been checked in the first four or five weeks of this year. This rate of deflation can not continue if we expect our financial and business structure to weather the storm.

As a result of the innumerable bank failures, bank depositors throughout the country, nervous and alarmed, have withdrawn their deposits from their banks at a rapid rate, in many cases solely for the purpose of hoarding. We estimate that over \$1,000,000,000 of currency was withdrawn for this purpose in 1931. Unfortunately, it is still continuing. Furthermore, this panic is not confined solely to domestic depositors.

Shortly after England abandoned the gold standard there were wild rumors all over Europe and the rest of the world regarding the banking situation in the United States and the possibility of our abandoning the gold standard. As a result of foreign withdrawals, over \$700,000,000 of gold was withdrawn from the Federal reserve banks for export or earmark in a period of six weeks during September and October. While those withdrawals were then checked, they were revived about the middle of January, and we are now in process of losing gold again.

Thus you will see that the reserves of the Federal reserve system are being pressed both from within and without. It was with this in mind that in recent weeks I had several talks with you, hopeful that you might see fit to include in your bill, not then published, some liberalization of our so-called free-gold position. Because of existing collateral requirements we were in the somewhat paradoxical position of having \$1,800,000,000 of gold in excess of our minimum reserve requirements, but in fact having only approximately \$450,000,000 of free gold. This margin, it seemed to me, was entirely too low, in face of the continued withdrawals of currency by domestic depositors and the continued withdrawals of gold for foreign account.

During one of my talks with you, you were good enough to suggest that I try my hand at drafting an amendment which would enlarge our collateral provisions, and I later submitted to you a proposal which I believe to be most important in the emergency with which we are now confronted. This proposal, while simple enough in its terms, is so complex and technical in its nature that it would require too much space adequately to discuss it in this letter. I shall therefore try to prepare for you a supplementary memorandum on that subject alone. I am not at all unmindful of the need of protecting the currency of the country from the risk of unnecessary or arbitrary expansion, and do not believe that the proposal I have given you will of itself run that risk. On the contrary, I believe the proposed amendment might well tend to defeat other much more radical proposals from an ever increasing number of inflationists.

Evidently, however, you concluded that it was not wise or practicable to include in your original bill a proposal along the lines which I submitted, so that that bill not only does not provide for the much needed liberalizing of the collateral requirements, but in fact, as published, it would, if applied to our present holdings of discounted paper and bankers' acceptances purchased in the open market, more than wipe out the existing \$1,300,000,000 of excess gold reserve.

This would be accomplished by two changes in the law proposed in your bill; the first no longer permitting gold held as security for Federal reserve notes to be counted as part of the 40 per cent gold reserve against outstanding Federal reserve notes (this of itself would reduce our excess gold to \$250,000,000); and the second eliminating from eligible collateral for Federal reserve notes member-bank 15-day advances secured by Government securities and also eliminating certain types of bankers' acceptances which we purchase in the open market. These two provisions alone would, in my judgment, render the Federal reserve system incapable of supporting continued withdrawals of currency and gold and would make it impossible for us effectively to carry on, pending a change in conditions or sentiment which would check withdrawals of deposits both by domestic and foreign depositors.

One other subject that we have discussed from time to time in the past is the possibility of enlarging the eligibility provisions so that member banks would be entitled in cases of need to borrow on assets not now technically eligible. The last time we talked about this in your office, prior to the publication of your bill, you mentioned to me quite privately that you had incorporated a provision which would enable groups of banks in an emergency, through some sort of combined liability, to seek accommodation from the Federal reserve banks. I said then that I felt that that provision would be most helpful in emergencies involving entire communities. I did not feel, however, that it would be of much practicable help to the individual bank, especially those located in the smaller communities, which has been subject to large withdrawals of deposits, which has already used up all of its eligible assets and which needs still further accommodation. Any small bank in this position in an isolated community would find it difficult, if not impossible, to form an association of 10 banks without running either the risk of too great delay or the risk of closing the bank because of advertising the very emergency which forced it to seek the or-

ganization of the group. But, even with this limitation, I felt at that time that your proposal for group borrowing would be helpful and as supplemented by the then proposed Reconstruction Finance Corporation, would probably be adequate.

I still feel that with your provision regarding group borrowing somewhat modified, to satisfy practical requirements, and with the facilities which the Reconstruction Finance Corporation will afford, there is not nearly the same pressing need now for an extension of the eligibility provisions of the act as there was at the time I first discussed this subject with you. Even so, I can not avoid the conviction that there should be some provision in the law which would make it possible for a Federal reserve bank, under appropriate restriction and regulation by the Federal Reserve Board and during temporary periods when the public interest requires, to extend accommodation to individual member banks, in case of need, upon assets not now technically eligible and at rates of discount at least 1 per cent higher than the prevailing discount rate on eligible paper. I think that such an emergency provision would do much, especially at a time such as the present, to relieve the minds of both banker and depositor and that it might be adequately safeguarded so as to avoid abuse.

This covers the two principal matters about which I have been most concerned in the past and on which I have felt it was important to have some early legislation.

Regarding the various and particular provisions of your bill I would prefer not to make any specific or detailed suggestions at this time or until you and Senator Walcott have proceeded further with Doctor Goldenweiser and Mr. Burgess. Most of the provisions on which I might wish to comment now will, no doubt, be discussed with them and possibly modified or eliminated, so that my comments at this time would be premature. But it does seem to me that, apart from the many drastically deflationary features in your bill which I have already briefly discussed with you and your committee, there is one broader subject that in the long run may become a matter of great significance to the system and to the country at large.

It is evident that many provisions of the bill are designed further to limit the autonomy of the individual Federal reserve banks and to concentrate more and more power in the Federal Reserve Board. I can not but believe that the purpose of the original Federal reserve act to create 12 autonomous Federal reserve banks, each managed by its own board of directors through officers appointed by those directors and subject only to general supervision of the Federal Reserve Board, was wise and sound. Any substantial departure from that fundamental principle might, I believe, ultimately result in seriously impairing the usefulness of the system.

Now, it is no doubt true that because of the fact that the New York Federal Reserve Bank is located in the most densely populated area in the country—an area in which are concentrated approximately one-third of the banking resources of the country—and because it has its principal office in the chief money center of the country, it will of necessity perform a disproportionate share of the work and bear a disproportionate part of the responsibility in connection with certain phases of the system's operations.

This is particularly true, of course, as to the handling of accounts with and from foreign central banks of issue, as well as to open-market operations in both Government securities and bankers' acceptances.

As to the foreign accounts, it should be pointed out, however, that the Federal Reserve Bank of New York has never sought or solicited the opening of any account from any foreign bank or banker. No such account has ever been opened with us nor has a reciprocal account been opened by us abroad without the affirmative approval of the Federal Reserve Board. Furthermore, the terms and conditions on which we do business with all foreign banks have been specifically approved by the Federal Reserve Board in advance of our opening any account. In addition to this general approval we have always and without exception submitted to the Federal Reserve Board for its approval every credit arrangement which we have entered into with any central bank. All accounts and all credit arrangements which we have opened or entered into with the approval of the Federal Reserve Board have been participated in by each of the other Federal reserve banks of their own choice.

Thus, all of our foreign transactions, even the day-to-day routine transactions, have been in accordance with agreements previously approved by the Federal Reserve Board, and every special engagement or arrangement has had the specific approval of the Federal Reserve Board, to which the fullest informa-

tion is forwarded currently about all of our operations with or for foreign account. This is as it should be. More than this, however, I do not believe to be practicable or feasible.

Foreign central bank operations, especially exchange operations, are difficult and technical operations, and must be handled promptly and expeditiously by men trained in foreign exchange and international banking business. If they are made subject to any greater or more direct control of the Federal Reserve Board or to the supervision of the open-market committee, as provided in your bill, our handling of those accounts will become practically so difficult and so cumbersome that they will in all likelihood be forced to private banking institutions in New York, outside the Federal reserve bank, where we will lose all the very real advantages of the present contacts and the value of the information afforded by those contacts. I can not overemphasize the importance of those advantages to the proper functioning of the reserve bank in the principal money center of the country.

So also I believe that the provisions of your bill relating to the open-market committee which is given jurisdiction over operations in bills as well as Government securities, are so cumbersome as to be inimical to the best interests of Federal reserve operations. A general clause leaving these matters subject to rules and regulations to be imposed by the Federal Reserve Board is, I believe, all that is necessary or wise. But the terms of your bill relating to open-market operations in Government securities and bankers' bills practically make expeditious and effective operations by the Federal reserve banks impossible in these two fields of action. The bill requires approval not only of the Federal Reserve Board but of a committee of 12 representatives of the several Federal reserve banks. It takes from each Federal reserve bank any individual powers, thwarts initiative, and leaves to the Federal reserve banks only the powers of obstruction. Under the proposed bill no operation in securities or bankers' bills, even the day-to-day transactions, can be effected, even in cases of emergency, without approval of the committee composed of representatives of the 12 reserve banks and of the Federal Reserve Board, and this approval must then be submitted to the Federal Reserve Board for its approval, and later to each Federal reserve bank as to its own participation. The powers of the directors of any individual reserve bank are thus reduced to the most insignificant proportions. Even the selection of the representative appointed by any individual Federal reserve bank to the open-market committee must be confirmed by the Federal Reserve Board.

I can not avoid the belief that ultimately the greatest protection which the system will have against political control or abuse is the maintenance of a fair measure of autonomy in each of the Federal reserve banks. To the extent that your bill further shifts power and authority from the Federal reserve banks to the Federal Reserve Board, to that extent, I believe it aims toward centralized operation and control through a politically constituted body in Washington. While I feel sure that the Board has not been dominated by political influences in the past, that danger is unavoidably an ever present one and would be materially accentuated by many of the proposals in your bill.

The best safeguard against possible political control, which I believe the Federal reserve act was originally designed above all else to avoid, is in the board of directors of the several Federal reserve banks. At the present time service on the board of directors is regarded as a privilege and an honor. Each reserve bank is in a position to call upon the most outstanding men in this community. But if they are to be merely conduit pipes through which recommendations of the Federal reserve bank officers will go to the Federal Reserve Board in Washington for advance approval, we can not expect, over a period of time, to be able to call for the service of the types of men who should be the directors of a Federal reserve bank.

For that reason, if for no other, I think the provisions of the bill, which further and further centralizes authority in Washington, will ultimately risk impairing the full usefulness of the system. To my mind, they are fraught with the gravest risk to the system. The bill eliminates the Secretary of the Treasury from ex officio membership on the Federal Reserve Board. That, no doubt, was purposed primarily to remove the Federal Reserve System from the possible taint of political pressure. But so many other provisions of the bill aim to increase the power and authority of the Federal Reserve Board, composed entirely of members who are political appointees, that it might well result potentially, at least, in a far greater centralized political

influence than is possible at the present time, even with the Secretary of the Treasury a member of the Board.

One more comment I would like to make and that is this: As I think I stated before your committee about a year ago, much of the banking trouble which we are now experiencing is due not so much to violations of law as to mismanagement within or abuse of privileges afforded by the law. Competition between the State and National Governments to liberalize the banking laws has gone further and further to make these legalized abuses possible. Limitations and restrictions in the law intended as safeguards against bad banking are too often regarded as invitations to unwise banking within the law. I am afraid that no matter how well a law may be conceived and drafted, that danger will always be present unless the management of individual banks is of the highest type. If, therefore, it is not possible at this time, either for practical or political reasons, to provide for one banking system which would include all commercial banks, as I would favor, then it seems to me that one of the most important contributions the proposed bill can make will be to insure better and better management.

With this in view might it not be appropriate for your committee further to consider some modification designed to insure better management in fact quite apart from legislative limitations and restrictions, such, for instance, as (a) reducing the number of directors on each bank so as to concentrate responsibility and to encourage supervision and management through experienced directors; (b) provision, under adequate safeguards, for the removal of incompetent bank officers after thorough investigation by disinterested authorities, and possibly (c) restriction upon the right of bank officers to borrow except with the approval of the appropriate committee of directors.

These and possibly other suggestions might be considered as a means of insuring a more conservative and effective management of banks within the limitations provided by law. No law, however perfect in itself, can serve as a substitute for management of individual institutions. And with a dual competitive banking system the legislative restrictions often prove inoperative in any event. If too strict in one system, banks shift to the other. If too lenient because of the competition for membership, they sanction bad banking. Ultimately, therefore, the protection of bank creditors and the community must depend largely upon the character and experience of bank management.

Very truly yours,

GEORGE L. HARRISON.

The next witness is Mr. Kent.

STATEMENT OF FRED I. KENT, DIRECTOR OF THE BANKERS TRUST CO., SCARSDALE, N. Y.

Mr. KENT. Mr. Chairman, may I ask your indulgence until I get this machine up? [Referring to hearing device.] I have to listen by proxy. I think I will be able to hear you now without difficulty.

The CHAIRMAN. Give your full name and your address to the reporter and state whom you represent, as well as whom you are connected with.

Mr. KENT. My name is Fred I. Kent. My address is Scarsdale, N. Y. I have, in a statement which I have prepared, mentioned at the start the few matters with which I am connected that I think you would like to have.

The CHAIRMAN. You are an officer of some banking institution?

Mr. KENT. I was for a number of years. At present I am a director of the Bankers Trust Co.

The CHAIRMAN. Of New York?

Mr. KENT. Of New York; yes.

The CHAIRMAN. You may proceed.

Mr. KENT. During recent years I have not been engaged in active banking, although I am a director of the Bankers Trust Co. of

New York, but have given my time largely to the study of matters having to do with the welfare of our people and particularly those things upon which they depend for their better living, that have to do with industry, trade, and agriculture, and the processes, financial and otherwise, under which they are carried out. Such studies have been aided through my connection with many organizations which have afforded me the opportunity to keep in touch with the growing movements of business.

For a number of years I have been chairman of the commerce and marine commission of the American Bankers Association, a member of the executive committee of the National Industrial Conference Board, the finance department of the Chamber of Commerce of the United States, and a member of the executive committee of the American section of the International Chamber of Commerce.

The business of merchants I have followed through the Merchants Association of New York and my membership on the banking and currency committee of that organization. Between all of these organizations and others in which I have membership, I have been able to follow closely developments having to do with industry, trade, and agriculture in the United States, with international developments of a similar character, and with financial operations. This being true, I have endeavored to measure the Glass bill from the standpoint of my general experience and my belief based upon such experience as to such values as it might have if it were enacted into law. Other witnesses here have gone into the detail of the bill at great length, and it would not seem necessary for me to do so. Such values as I can carry in its consideration should have greater bearing upon the general effect of the passage of such a bill than upon its detail, and I will therefore confine myself to such consideration.

In view of the fact that I am opposed to the bill and must take a position against it on that account, I would like to say that in doing so, my criticism is based entirely upon the provisions in the bill and the effect that they can be expected to have upon conditions as they exist at the moment, and not upon the intent of the sponsor for whom I have the utmost respect.

It would seem necessary, if we are going to meet intelligently the problems of the future, that we weigh carefully the effect of any legislation that might be under consideration, particularly as it may have a bearing upon the banking system of the country with possible unfavorable repercussions upon industry and trade.

The Glass bill, if it proved to be deflationary as I and so many others believe would be the case, would, if enacted into law, tend to add to the depth and duration of the depression and probably to an extent that might create further unemployment of a devastating character.

Regardless, therefore, of whether the Glass bill is sound in principle, it clearly is against the interest of the whole people of the United States to have it enacted into law before there has been a very substantial recovery from present conditions and a period of normal stability has been attained.

But is the bill sound in principle? Would it carry into our banking system a force for good even if its enactment were postponed until industry and trade were again upon solid ground?

There would seem only one answer to such a question, and that is that it would not. Back of its provisions which have to do with its apparent principal purpose, it ignores our industrial financial system as it has been built up and as it exists and as it must be carried on until we have some better system, if one can be devised to take its place.

Does the Glass bill even attempt to provide a better system? No. It would merely destroy in part our present system and provides nothing in its place.

Let us analyze this statement and see why it is so:

Present-day industry and trade are financed in two parts, by capital or capital issues, and by bank borrowings. Capital financing is utilized to provide for plant, for required long-time turnover, continuing inventories of raw materials and of processed goods and for margin of safety.

Bank borrowing is resorted to for seasonal requirements, purchases of raw materials which quickly move into finished goods, finished goods on short-time carries, raw materials, and finished goods in transit from buyer to seller, and for other short-time purposes.

The general and ordinary financial structure of industry is therefore in the form of securities—stocks and/or bonds, or cash or other securities, and commercial paper; that is, trade paper, or book accounts between business houses, and notes to banks.

There are five classes of bank deposits: Two from cash, demand and time, or saving; and three from credit: Loans, rediscounts or sale of paper taking time to collect.

The security structure of industry and trade, as it is built up, is exchanged for cash which is received from a multiple of savings and time deposits when banks become holders except, for their capital investment account, and from cash or demand deposits when individuals, firms, or corporations become holders.

Industry and trade can not, however, find those who may be willing or anxious to become holders of their securities unless they depart from their regular business and enter into the business of financing. This they could not do except at enormous expense for an occasional issue, nor would they be able to assure themselves of round sums so essential at times for needed expansion of plant or other facilities if they would hold or create markets for goods.

The banker, therefore, becomes necessary to industry and trade in placing securities as well as in loaning funds for reasonable purposes.

Placing securities requires underwriting in part and, most important of all, a market in which buyers may sell in case of need or desire. Without such a market, finding buyers would be worse than trying to carry on world trade under barter.

But a market for securities requires capital and it also requires both buyers and sellers who operate to distribute and not to hold. Such persons handle securities as merchants do commodities. Those who buy do so with the expectation of selling at a profit commensurate with the risk. Those who sell long or short do so with the expectation of buying again at a profit commensurate with the risk. The farmer plants and grows his products hoping to sell at a profit and he does so at a risk; the manufacturer buys raw materials, pays for labor, and produces goods for which he hopes to get profit,

but he does so at a risk. Buyers and sellers of securities and commodities operate knowing that there is risk.

As commodity and security prices rise, the profit to those who in their business buy or create first becomes greater with the same turnover. But as such prices reach abnormal heights, risks increase and borrowing for purchase of land, commodities, or securities, becomes fraught with growing danger.

As prices fall after the turn from high prices, those who buy first on judgment or necessity lose margins of profit expected or planned for in the same proportion, or make further losses if price movements are rapidly downward.

But mankind must live whether prices are going up or down and so production and distribution of many things are going on at all times.

The normal growth of production has been found over a period of years to be about 3 per cent annually. The destruction of capital due to the vicissitudes of business operation, caused by errors in judgment, catastrophe, invention, discovery, or changes in the habits and customs of the people, together with the 3 per cent in increased need, requires the issuance of new securities for capital used in substantial sums year in and year out.

If the facilities which have been created through banking operation for such issues were to be unduly restricted because a wave of extravagance passed over the nations and affected those in every walk of life, that is, in Government, in finance, in industry, and in and out of all business, we will pay the penalty through continued unemployment.

Discrediting securities as collateral because prices are down during a depression that is partly cyclical but whose depth and duration are now largely due to unfortunate world political forces, is not only unwise but would be positively suicidal.

Shall we say that all government is evil because men in government office have made mistakes? Shall we strike at all industry because men in industry have made mistakes? Shall we unduly curtail forms of banking, upon which both government and industry depend for their ability to derive income, because some bankers have made mistakes? All men were under the same pressure during the period preceding November, 1929, and judgments were hard to render. This, however, had nothing to do with the normal values of sound securities. Neither did the fact that men and women in all walks of life were speculating in real estate, commodities, production, or securities, because human nature would have it so.

Industry and trade require, and will continue to require, funds from securities and funds from banks. The proportions must be sound. Federal reserve examinations are intended to insure the maintenance of such soundness on the part of those who borrow from the banks in the system and in the asset structure of the banks themselves.

No group of men has the intelligence to measure in legislation what is going to be the satisfactory and most effective use of banking capital month in and month out during the coming years. The judgment of banking men must be allowed to prevail within reason

currently with regard to the operating needs and policies of the moment. Bankers are human beings and they have made mistakes the same as other men, but they have done nothing to warrant the abuse that has been heaped upon them recently to the great detriment of our whole people. They have had to bear the burden of the most trying conditions that bankers have ever faced and lived through, and they are ready in tremendous proportion to meet the needs of industry as they may arise during the reconstruction period that all business is hoping will be allowed to set in by governments.

As proof of the statement of the needs of industry for corporate issues we only need to refer to the amounts of new capital issues in the United States for such purposes during recent years. For the five years from 1919 to 1923, inclusive, the average issues per year were \$2,300,000,000. For the five years 1924-1928, inclusive, they were \$4,600,000,000. In 1929 they were \$8,639,000,000, in 1930, \$4,944,000,000, in 1931, \$1,763,000,000. The falling off from 1929 to 1930 and from 1930 to 1931 clearly tells the story of reduced production and reduced business activity.

These new capital issues were to meet the needs of the railroads, the iron, steel, coal, and copper industries, equipment manufacturers, motor, and accessories, rubber, and a few other producers' goods, and public utilities, and many other lines of consumers' goods. The funds were needed to carry on the trade and industry of the country with the same force that bank loans and rediscounts were required.

January 1, 1929, the average quotation of all American bonds on the New York Stock Exchange was 98 per cent. March 1, 1932, the average was 82 per cent. The market value of these securities on January 1, 1929, was \$29,177,875,514, and on March 1, 1932, \$27,318,668,023. In addition to American bonds there was outstanding in market values in March, 1932, on stock issues \$27,585,969,257 and in foreign bonds, \$12,028,382,077. This mass of securities representing altogether \$67,000,000,000 in round figures, even under present conditions, is evidence of the value to the holders of a positive security market.

It is not conceivable that such a market could exist if every natural channel through which funds are applied to maintain it was stopped up or curtailed through legislation. The securities listed carry income to the people, to partnerships and corporations. Industry and trade in sufficient volume to meet the living needs and further the desires of our 120,000,000 people have only been possible because of the placing of these securities. Dealing in them carries neither disgrace nor should it carry criticism under normal conditions. The protection of our security market, the utilization of the funds which go into it and the buyers and sellers who take part in it are essential activities in connection with the other processes, financial and otherwise, of industry and trade.

So-called banking affiliates were created to meet an actual need and for the double purpose of furthering the security business for the benefit of industry on one side and of investors on the other, and at the same time provide sound channels through which securities could flow clearly separated from wild-cat issues. The fact that security values, together with all other values as expressed in money, have fallen because of the depression, and that reduced earning power due to the depression in business, has vitally affected the

standing of many securities, does not offer grounds for criticism of those engaged in the security business. At the moment we are all vitally concerned, in Government and out, in the reestablishment of business on a basis that will absorb the unemployed and restore normal values to all of those things which represent wealth and tokens of wealth. If such reestablishment is to proceed with sufficient movement to protect our people, it is essential that the issuance of securities and the security markets be protected and regardless of whether following the return of normal times, it may be found desirable to make some changes in methods of handling securities, there would not seem to be the slightest doubt but that it would be a great mistake to undertake anything of the kind at the moment.

For many years Senator Glass has been striving to find ways to prevent times of excessive speculation from developing that might be harmful to the people. Bankers throughout the country, almost without exception, have recognized the earnestness of his desire and the fine intent back of it. But the problem is one of human nature and reaches throughout mankind almost from the cradle to the grave. The small boy loves to speculate in the little ways that opportunity offers. Almost every act of man has a speculative side and its control is at times seemingly beyond power.

If there is a way to prevent the recurrence of the conditions which prevailed during and since 1929 by legislation or otherwise, it should be found. But there would seem grave doubt, based on the experience of mankind, to what degree it is possible to provide sound corrective legislation during a period of strain and stress with all the forces that are brought to bear upon legislators by those enduring hardship.

Regardless of any other point of view, therefore, it would seem unwise to attempt any corrective legislation attacking the fundamentals of business and financial operations as they now exist until the present depression has run its course.

The CHAIRMAN. Do any members of the committee want to ask any questions?

Senator GLASS. I do not.

Senator BROOKHART. Mr. Chairman, I believe I do. I notice in your statement that you say the wealth increase of the country is about 3 per cent.

Mr. KENT. No; the production.

Senator BROOKHART. The wealth production?

Mr. KENT. I was referring particularly to the physical production. It increases about 3 per cent.

Senator BROOKHART. That is 3 per cent upon what was in existence at the beginning of the year?

Mr. KENT. Yes.

Senator BROOKHART. And you add 3 per cent more to it at the end of the year?

Mr. KENT. Yes, sir.

Senator BROOKHART. Does that represent the history of the country?

Mr. KENT. It was measured by one of the statistic companies. They cover a period of several years. I think it was something like 10. They came to the conclusion from their figures that that was about the average movement.

Senator BROOKHART. In the course of a period of 10 years it would depend a good deal on which 10 years you would select. From 1912 to 1922 the census shows about $5\frac{1}{2}$ per cent.

Mr. KENT. Per year?

Senator BROOKHART. Yes. But from 1912 to 1928 it is cut down to about $4\frac{1}{4}$ per cent.

Mr. KENT. Yes; that is true.

Senator BROOKHART. And from 1912 up to date it is cut down probably to your 3 per cent.

Mr. KENT. Yes.

Senator BROOKHART. From a long study of it I have figured out slightly less than 4 per cent.

Mr. KENT. Well, I have seen it stated as 4 per cent. I happened to use the figures of the standard statistics because I thought we might just as well be conservative. I have seen it stated 4 per cent.

Senator BROOKHART. That means, then, that the net income of our country over all operating expenses, living expenses, and waste of competition, and all that stuff, is about, we will say, 4 per cent?

Mr. KENT. This percentage is not based upon income; it is based upon physical production.

Senator BROOKHART. I understand, but income is the physical production. That is all there is to it, when you simmer it down.

Mr. KENT. It is a little different percentage when translated into dollars.

Senator BROOKHART. I mean the income now of the whole people, all labor, all capital, all everything that goes to make it up.

Mr. KENT. The income of the whole people has changed very materially. It was figured out very carefully as being \$71,000,000,000 in 1930 and \$60,000,000,000 in 1931.

Senator BROOKHART. Yes; but out of that must come living expenses.

Mr. KENT. Yes.

Senator BROOKHART. And operating expenses.

Mr. KENT. Yes; exactly.

Senator BROOKHART. And waste of competition, which is a tremendous item; and that leaves when we get down to it this 3 per cent that you figure it, and I figure it something less than 4 per cent.

Mr. KENT. Over a period of five years, including 1928, the amount of income that went into securities averaged about \$600,000,000 a month; that is, into securities and also savings accounts, which meant that there was that amount left after all of these other things you speak of were carried out.

Senator BROOKHART. Yes; I understand that went on the books, but were not those securities necessarily watered and inflated in order to render—

Mr. KENT (interposing). No; not necessarily. The idea of water in securities is not entirely clear from the standpoint of what actually happens when securities are issued. Suppose a concern issues new capital and receives a million dollars for it. It receives a million dollars for capital, and it has that in cash. It utilizes that capital to increase its plant or to increase its facilities to process or to distribute, and so forth. Now there is no question of water there.

Senator BROOKHART. No; but supposing it would issue \$2,000,000 of stock and a million dollars of bonds then against it. That would be water.

Mr. KENT. It makes no difference. No; there is necessarily no water there.

Senator BROOKHART. That is what I call water, anyway.

Mr. KENT. It depends upon what you utilize it for, or whether you carry it out in such a way that you have a full return, a hundred per cent return for your investment.

Senator BROOKHART. Now, then, coming down to this proposition: If capital got all the wealth it possessed in the country it could not, on your figures, on a broad distribution, get over but about 3 per cent, could it?

Mr. KENT. Well, no, not exactly; because that 3 per cent to which I referred was not 3 per cent in dollars, but I think if you will look at it in this way, Senator Brookhart, there is a great deal of capital destroyed every year, for the reasons which I stated, the vicissitudes of business, catastrophe, change.

Senator BROOKHART. Waste of competition?

Mr. KENT. Yes. Well, from all the reasons that develop. Changes in the habits and customs of people make tremendous differences, and new inventions and discoveries destroy certain lines of business.

Senator BROOKHART. It has been estimated by Senator Pepper that 92 per cent of American business ultimately fails. Do you agree with that?

Mr. KENT. Well, "ultimately" is a long time.

Senator BROOKHART. The average is less than 10 years. That is not so long.

Mr. KENT. That is pretty hard to say, because there are consolidations and changes going on in business. An invention will come in and a man will change his business from doing that which he is doing to something else. That business disappears. That may be part of your 92 per cent, but it may be perfectly sound.

Senator BROOKHART. That would not be listed in the 92 per cent; that would be in the 8 per cent.

Mr. KENT. I am not so sure that it is possible, with statistics as they are, to make any such differentiation.

Senator BROOKHART. You mentioned now, and your line of argument is, that nothing ought to be done to disturb this sound system of business of ours. Colonel Ayers in here the other day showed that we had had 8 major depressions in the last 50 years. We have been at no time at all in a normal line. We were either going up in inflation or coming down in deflation.

Mr. KENT. Well, that comes about on account of human nature, which seems to be unavoidable.

Senator BROOKHART. Now, let us see about human nature, that phase of it. You concede that this stock gambling and betting on stocks has something to do with this up and down business in our country, do you not?

Mr. KENT. It would occur anyway in commodity prices.

Senator BROOKHART. The stock exchange could not operate unless it could use the mails and telegraph, could it?

Mr. KENT. I think that is probably right. They would have to operate on the ground.

Senator BROOKHART. That is one element of human nature we could take out entirely by law?

Mr. KENT. If you wanted to destroy industry; yes.

Senator BROOKHART. If we wanted to destroy gambling, the speculation there.

Mr. KENT. I do not think you can destroy gambling while any of us live.

Senator BROOKHART. Another way: We could levy a tax on these speculative sales where they were reselling within 60 days high enough to stop them.

Mr. KENT. And even then, you might destroy business. Now, the reason I say that, Senator—

Senator BROOKHART (interposing). Your idea is that this business must fluctuate up and down; that we can not get along without the gambling feature of it?

Mr. KENT. If you say that a man who buys goods and puts them in his store at a certain price expecting to sell them for a higher price is gambling, I would say yes.

Senator GLASS. You do not differentiate that from standing at a ticker and betting what will be the state of the market in a half an hour?

Mr. KENT. It is different. Standing in front of the ticker is done on a different character of thought than I have in mind. But what I mean is this, Senator: It is necessary that there be a market for securities, because if there is no market for securities, the capital structure of industry can not obtain the funds that it needs and bankers would not be able to loan to industry unless its capital structure was sufficient to act as a margin of safety.

Senator GLASS. Nobody denies that proposition.

Mr. KENT. So you must have a market for your securities.

Senator GLASS. I say nobody denies that proposition.

Mr. KENT. Yes. Well, then, it means that you must have a market for your securities, and in the market for securities you have men who buy securities, no matter whether they want to keep them or not, because they are hoping that the trend of conditions is such that they will be able to sell them at a higher price. That is exactly what the merchant does.

Now, you know, as I do, that in commodities and merchandise as well as in stocks times occur when those engaged in the business load up when they should not. You will find that many merchants buy things and put them on their shelves at prices that are so high they can not turn them over, and they buy large quantities when they think that there is going to be a rising-price period. That is the natural way that happens when they buy large amounts.

Senator GLASS. You think that there can be no definite distinction between "investment" and "gambling"?

Mr. KENT. No definite—no; I do not say that. I do not call it gambling. You and I have possibly a different idea of gambling. I do not consider that every man in this United States who buys something before he sells it, whether it may be goods or whether it may be raw materials to manufacture, or whether it may be labor to apply to that manufacture, or whether it may be securities, is gambling.

Senator GLASS. He sometimes affects to buy things which he does not buy, and many times sells things that he does not own; isn't that true?

Mr. KENT. There is no difference. You must have short selling in order to have a market that will make it possible for those who have securities to sell their securities upon need at any moment, a situation that carries a free market; and when men sell stocks that they have not, they borrow those stocks and they owe those stocks to the people from whom they borrow, exactly as a merchant would borrow money from a bank to buy commodities.

Senator GLASS. Mr. Kent, I hope you do not think I have ever been simple enough to suppose that I could put a stop to gambling.

Mr. KENT. No; I think you have a very high purpose in trying to control it in so far as is possible.

Senator GLASS. But I have judged from your statement so far that you think we made a grave mistake, if not in a moral sense, certainly in an economic sense, to have ever instituted the Federal reserve system. You think we made a grave mistake in withdrawing the reserve funds of the country from the stock speculative market?

Mr. KENT. I think the Federal reserve system is a wonderful system, very finely conceived, and I think it is of tremendous value to the people of the United States. I think it is of value to the whole world as a stabilizing influence.

Senator GLASS. If you think stock speculation, as you call it, and stock gambling as I call it, is essential to the prosperity of the country and the sound conduct of the banking business, why should we have ever withdrawn the reserve funds of the country from the financial centers and impounded them in 12 Federal reserve banks and textually by law precluded their use for stock-speculative purposes?

Mr. KENT. That purpose, as it was carried out in the Federal reserve system was not, as I saw it, in 1913, when the Federal reserve bank was being worked out, the main purpose. The situation as it existed before the Federal reserve system was organized was that banks throughout the United States had funds, we will say, in New York banks that they placed there at the time of year when they could not utilize them in their own part of the country, in their own localities. Those funds were accumulated in the New York banks. New York banks, in order to pay interest upon them and give the return to the country banks that the country banks desired, were obliged to loan those funds somewhere. What did they do with them? Some of them they loaned against collateral security, stock exchange security, and they never lost a dollar on the stock exchange securities.

Senator GLASS. I am not talking about the security.

Mr. KENT. No; I know. Some other funds were carried to other countries and were loaned in England and in France and in Germany. Then, when the fall movement came on and the country banks desired their funds, they would send to New York for those funds and New York in turn would send for them to London and import gold in order to be in position to protect the banks out in the country, and it was found that at times there would be such a demand upon the New York banks for funds all at once that it made it very difficult or impossible for them to meet those demands in a

way that was advisable in order to protect the country, and we had the development in 1907 when the banks throughout the country began to be fearful about their reserves and they withdrew the balances that they had in New York, not because of their fear of New York banks, but because of their fear that so many might be asking for money at the same time as to result in strain and so they began to withdraw theirs.

Now, what happened? As I recall it, I saw these figures in December, 1918, the banks in Georgia had 180 per cent in cash more than their reserve required, and the banks in other States throughout the South and the Middle West had a tremendous amount of cash above their reserve requirements, and they not only withdrew their balances from the New York banks, but they borrowed money from the New York banks in addition, which they withdrew in cash also, and built up cash reserves in their own banks for self-protection; that made it very difficult and the New York banks had to go on a clearing-house basis.

Now, that was not a sound situation to have developed. The Federal reserve system organized as it is now, has done away with the menace of that situation. It has made it possible for the bankers in the country to obtain funds when they need them, regardless of how investments were carried out.

Senator GLASS. That is simply the historical technique of the organization. That has not been the only purpose of the Federal reserve banking system. Why, do you think, when we delegated to the Federal Reserve Board the exclusive right to define eligible paper affirmatively for agricultural, commercial, and industrial purposes, and then negatively prohibited such definition to comprehend speculative investments, stocks and bonds, notes and bills drawn for speculative purposes—why do you think we did that when we drafted the Federal reserve act?

Mr. KENT. At that time I remember there were many speeches made against the use of the funds of the country on the New York Stock Exchange, and that undoubtedly was in the minds of many Congressmen when the bill was passed.

Senator GLASS. The law provides that to-day, does it not?

Mr. KENT. The law provided it. But the eligible paper has proved to be insufficient, and the Glass-Steagall bill has recently been passed in order to make it possible for the country to save itself against this depression, and the conditions which have developed under it, because there is not sufficient eligible paper at the moment.

Senator GLASS. I put into the record here on yesterday, I think, the latest report from the Federal Reserve Board itself, which definitely stated that there is ample eligible paper for rediscounting, giving the volume at approximately \$3,000,000,000.

Mr. KENT. Yes.

Senator GLASS. Somewhat under that amount, and added a statement that it was fairly distributed throughout the country.

Mr. KENT. Well, it might be fairly well distributed and yet not be in the hands of those who need it most. But, of course, you have another situation there that has developed because of the depression that has made the banking situation much more difficult.

Senator GLASS. But aside from that, no matter what has been the change in the situation, the banks have not any right to violate the law, have they?

Mr. KENT. No; they have not.

Senator GLASS. If the law is unwise—

Mr. KENT (interposing). I do not know that the banks have violated the law.

Senator GLASS. If the law is unwise it ought to be changed.

Mr. KENT. If unwise, there ought to be a change. But I do not know of the banks having violated the law.

Senator GLASS. There is nothing in this bill that prevents banks from gambling away or speculating away, as you would prefer to say, every dollar of its deposits, is there?

Mr. KENT. A bank can do that regardless of law or anything else if a banker is in the mood to do it. You can not prevent that.

Senator GLASS. I say, there is nothing in this bill to prevent it, is there?

Mr. KENT. To prevent their doing it?

Senator GLASS. Yes.

Mr. KENT. In what way?

Senator GLASS. Well, just standing up at the ticker and betting on margin.

Mr. KENT. Of course, they can not buy stocks. The national banks can not buy stocks. Some State banks can, but that has nothing to do with this bill.

Senator GLASS. I say that has nothing to do with this bill?

Mr. KENT. No; that has nothing to do with this bill.

Senator GLASS. There is nothing in this bill that prevents a bank from doing anything it pleases with its own money, is there?

Mr. KENT. It would seem to me there are many cases that might develop where a bank could not do as it pleases in this bill.

Senator GLASS. There are many cases developed where a bank should not do as it pleases, are there not?

Mr. KENT. There are many more where a bank should be able to do as it pleases.

Senator GLASS. Well, perhaps so.

Mr. KENT. It is quite impossible to legislate either judgment or knowledge into a banker. He has to carry his business on based on his experience and in connection with the law as it exists. He should be given every opportunity to utilize his judgment in the ways that are necessary in order to further business.

Senator GLASS. Well, in the last analysis, then, you would believe, Mr. Kent, that there should be no legislative or regulatory restrictions upon the operations of a bank?

Mr. KENT. No, sir; I would not say that. As a matter of fact, I stated specifically here that if there is any way, through legislation or otherwise, to develop a situation following this depression that would have a tendency to prevent or would be helpful in preventing a new development in the future like that which occurred in 1929, that we should put it in force. We should study to find out what it is and then put it in force. But I do not believe that we should do anything at this moment that would be deflationary in character or might be deflationary in actual practice, when we are all striving

with every force that we can bring to bear to get out of this difficult situation.

Senator GLASS. Well, of course, there is a difference of opinion as to—

Mr. KENT (interposing). Oh, there would be, naturally. I realize that.

Senator GLASS. Whether there is anything of a deflationary character in the bill. But what I am trying to elicit from you, Mr. Kent, is whether you think it was unwise to set up the Federal reserve system and primarily in the beginning and to this day to have preserved the reserve funds of the country for the use of agriculture, commerce, and industry.

Mr. KENT. No; I think not, although I can easily see that in addition to that it might be of tremendous value to have in the law as a continuing force something that lies within the terms of the Glass-Steagall bill that would enable the Federal reserve board in case of emergency for the time that would seem necessary to meet that emergency to carry out the operations all through the Federal reserve banks that are covered in the Glass-Steagall bill.

Senator GLASS. We have that now. That is permanent law.

Mr. KENT. Yes.

Senator GLASS. Yes; we have that now. Nobody is particularly objecting to that.

Mr. KENT. I think it covers the question thoroughly.

Senator GLASS. I say, nobody is particularly objecting to that, though I very much doubt whether it has been largely availed of.

Mr. KENT. The ability to avail of it is the important thing, because that relieves the banker who is in a difficult position because of the drop in price of securities.

Senator GLASS. Another case of getting along with psychology.

Mr. KENT. Yes. And very positively, Senator Glass. You take these country banks and the banks in small towns, and they have been put in a very difficult position where they have had cash drawn out for hoarding and the value of their securities has gone down and the margin of safety in between has become very small, and they were fearful to make loans even if they had opportunities, but this Glass-Steagall bill gives them a freedom from that fear.

Senator GLASS. Yes; we understood that.

Mr. KENT. Because if they sell the securities now and the markets are down, they will have to take the loss, whereas if they can carry those securities until we get a turnabout, then they will not have to take a loss.

Senator GLASS. Yes; we understood that. That is why we drafted the so-called Glass-Steagall bill. Well, I am through, Mr. Chairman. Some of my colleagues rather deplore my combative tendencies anyhow. But when I hear and find presented and see what I think is rather glaring lack of logic, why, I just can not help but point it out. But I am through.

Senator BROOKHART. Mr. Kent, I wanted to ask you a little more about those security issues. You gave a total, I believe, listed on the stock exchange in 1920?

Mr. KENT. The figures that I gave you, yes; I gave for 1920, I think, and 1932.

Senator BROOKHART. What is the total, do you remember?

Mr. KENT. The figures that amounted to the sixty-seven billion represented the value in March of this year on the stock exchange, the quoted values.

Senator BROOKHART. What was the value in 1929, then, August or September?

Mr. KENT. The value in 1929, August and September—twenty-nine billion in the case of the bonds on the New York Stock Exchange, the domestic bonds. It was sixteen billion for the foreign bonds—

Senator BROOKHART (interposing). The total is what I called for.

Mr. KENT. I do not recall that I have seen the total valuation of the stocks separately. But those two bond figures would have been forty-five billion. That would leave the balance for the stocks, which was very much higher.

Senator BROOKHART. Some bonds increased in value from forty-five up to sixty-seven billion?

Mr. KENT. No; the sixty-seven billion includes the stocks in March, 1932. I did not give you the stocks in 1929. I may be able to think of those figures a little later, but I can not quite recall them at the moment. I do not know that I noticed them particularly.

Senator BROOKHART. The total of the whole thing was very much more than sixty-seven billion?

Mr. KENT. I am not so sure that it was not eighty-nine billion for the stocks at that time, in 1929.

Senator BROOKHART. And then about forty-five billion for the bonds?

Mr. KENT. That is including domestic and foreign; yes.

Senator BROOKHART. They were worth more than twice as much on the market then in 1929 as they were in—

Mr. KENT (interposing). No. Oh, no. The figures were 89 per cent on the American bonds in value in 1929 and 82 per cent in March, 1932. The foreign bonds were 96 in 1929 and they were 63 in 1932.

Senator GLASS. Now, that I have made my speech, I suggest that we get on, Senator.

Senator BROOKHART. You say this 89 represents the whole value of stocks, bonds, and everything?

Mr. KENT. No; only stocks and I would not give you that figure as being positive, because you are asking me the value of stocks in 1929.

Senator BROOKHART. If you don't remember it, we will not go into it.

Mr. KENT. My recollection is that their value was eighty-nine billion, and I know the values of the bonds. I am sure of that. The bonds themselves were twenty-nine billion and sixteen billion.

Senator BROOKHART. We will drop that, if you do not remember the total. How much did the stock exchange sell each day in August, 1929?

Mr. KENT. In shares? That ran up into many millions of shares on some days but that was a turnover back and forth.

Senator BROOKHART. And all of these issues that you described, these new issues, were sold to the public at large?

Mr. KENT. Yes. That is, they were distributed to the public, if you want to include some bankers all over the country as a part

of the public. Many institutions bought them, life insurance companies and others.

Senator BROOKHART. And they passed them on to the public?

Mr. KENT. Oh, no. Many of the bankers put them into their investment accounts.

Senator GLASS. They wish now they had passed them on to the public, do they not?

Mr. KENT. How is that?

Senator GLASS. I say, they wish now they had passed them on to the public, do they not?

Mr. KENT. Everybody wishes that everything that they have which is worth less now that it was when they bought it had been sold or that they had not bought it. But that does not change the value of those securities, Senator Glass. We are in a depression, and everything is down, and when we get out of this situation and commodity prices begin to move up and earnings begin to come back, then you will find that these securities are going to be reinstated.

Senator GLASS. When is that going to be?

Mr. KENT. It went up two points only last month.

Senator GLASS. When is that going to be?

Mr. KENT. Why, I have not fixed the date yet. That is what we want to have you do.

Senator BROOKHART. You say they are going to be reinstated. Don't you mean under this system they are going to be reinflated?

Mr. KENT. No; I do not see that it makes any difference what you call it. The point is that their intrinsic values are coming back. Many of these securities are quoted way under their intrinsic values.

Senator BROOKHART. Many of them are still above their intrinsic values, too?

Mr. KENT. Well, you may know as to that. I do not.

Senator BROOKHART. I have a chart of the Federal Reserve Board which shows them about 40 per cent above the 1914 level of values.

Mr. KENT. But that does not measure intrinsic values.

Senator BROOKHART. That was about 33 per cent above the next preceding level in 1904.

Mr. KENT. That does not measure intrinsic values.

Senator BULKLEY. What are "intrinsic values"?

Mr. KENT. Intrinsic values—suppose you have a bond that represents a first mortgage on a railroad that has 22,000 miles of trackage and the total value of the bonds outstanding on that particular issue, that particular first mortgage, is such that the intrinsic value would represent a certain value per mile.

Senator BULKLEY. What is "intrinsic value"?

Mr. KENT. "Intrinsic value" is what you might call the wealth price, I should think.

Senator BULKLEY. That does not make it any more clear to me.

Mr. KENT. Well, suppose you take—

Senator COUZENS. Take the Wabash Railroad, for instance.

Mr. KENT. Well, take a corporation. Suppose a corporation issues bonds and with the proceeds of those bonds it puts up buildings that cost a certain amount. Those buildings are kept in order and they have certain values. They could be sold for those values.

The bonds are entirely upon those buildings. Now, the intrinsic value of those bonds, if they cover the buildings and nothing else, are the first lien upon those buildings, the intrinsic value would be the value of—

Senator COUZENS. What is the value of the building?

Mr. KENT. The value of the building would not always be the same of course, the intrinsic value of the building might have been different some years ago or possibly some years hence. The value of the building depends upon what the people are willing to pay for it partly, and partly what they get from it.

Senator COUZENS. What would have been the intrinsic value of a brewery or distillery when the prohibition law went into effect?

Mr. KENT. Why, they may have utilized it to manufacture different things.

Senator COUZENS. But the intrinsic value before prohibition is different from what it is after prohibition, is it not?

Mr. KENT. Well, certainly.

Senator COUZENS. You can not define "intrinsic value" then, can you?

Mr. KENT. Now, wait a minute. You say it was different. It was different based on an earning power from the manufacture of liquor, but the earning power from the manufacture of something else that the building might have been utilized for, might have been even more than the return they got from manufacturing liquor.

Senator COUZENS. Yes; but let us take a railroad, for instance, that was built prior to the advent of the increase of the motor vehicle.

Mr. KENT. Yes.

Senator COUZENS. Is the intrinsic value the same now as it was then when it was built?

Mr. KENT. I should say not; but I do not think it is so much the motor vehicle as it is the expenditures of the Government for waterways that go into taxes and the taxes that are collected from the railroads and many things of that sort that have developed. I think that is more the trouble with the railroads.

Senator COUZENS. So the further you go on the less you are able to define "intrinsic value"?

Mr. KENT. Well, it means something. There is no question about it.

Senator GLASS. Mr. Kent, you have tempted me to break in again.

The CHAIRMAN. Senator Brookhart has quit. So it is your turn.

Senator GLASS. At one period of stock-market operations in New York in 1929, as I recall, though I will not be definite as to the figures, loans for others amounted to approximately seven billions of dollars.

Mr. KENT. Oh, no; three billion nine hundred million. I think that was the largest amount.

Senator GLASS. That figure will suit my purpose just as well as seven billions. How much of that money would you be willing to say was loaned discriminatingly and intelligently upon the intrinsic value of the stock?

Mr. KENT. Why, I would say that events since would prove that better than any opinion I might have. The total loans at that time was six billion. Now they are about five hundred and fifty million. They have all been paid without the loss of a dollar.

Senator GLASS. I am not talking about losses.

Mr. KENT. Yes; but the loans from others went to the stock exchange.

The CHAIRMAN. He means the banks did not lose that.

Senator GLASS. I know; I am not talking about what the banks lost; I am talking about the people who sent that money there to be bet on the stock market. How much of it was put up upon an intelligent understanding and discrimination of the intrinsic values of the particular stocks that it was levied against?

Mr. KENT. It was put up in two or three ways. You must understand I have never dealt in stocks, so that I have not the full details of the way they handle those things, except that I know this: Those who are requested to buy stocks by people who want to invest are told in large percentage what stocks they are to purchase, and they act as brokers and make the purchases for the people. Then, there are some cases where people confer with their brokers as to what stocks they should buy. Now, the brokers, in their own interest, prefer to have their clients make money. They do not want to put them into securities where they will lose if they can help it. But, unfortunately, in 1929 or previous to that, we had the capital gain tax, which was largely responsible for the high point to which the stock market went, for the reason that thousands and thousands of men did not take care of their investment securities properly and study them all the time and change them from this and that and the other security to try and keep their investment portfolios sound, because they saw if they sold they would take a loss, in the fixing of an income-tax obligation, and the result was they held their stock. They kept millions of shares of stock out of the market, so that, when people tried to buy stocks, there were fewer shares for them to buy. It made the market go up.

Then, another thing was that the Government received from the capital-gain tax large sums at that time which it never should have received, because that induces Government extravagance, and they were sums that did not represent real profit. If you buy a lot of stocks to-day and the whole stock market goes up 10 per cent and you sell them and then buy some other stocks, you have not made a profit, because the other stocks you buy are purchased on the same level as the ones that you sell. There is not any question of doubt but that the capital-gain tax was at the bottom of the high level that was reached in 1929.

Senator GLASS. Well, I simply despair of getting you to answer my direct question. If it is as difficult to answer it as it has seemed to be easy not to answer it, it can not be answered. What I want to know is, how many of these people outside of the metropolitan districts, who send their money there to be invested on the stock exchange, have any actual knowledge of the intrinsic value of the stocks they are dealing in on the stock exchange.

Mr. KENT. The intrinsic value of any stock, if you want to use the word—I know you do not like the word, but I do not know as it makes so much difference what word you use—

Senator BULKLEY. I like it, but I would like to know what it means.

Mr. KENT. I should say that the value would change. It must change, because the earning power of any corporation changes with

the developments in the commodity price level, and therefore what is back of the securities, that is, actual wealth, changes in the amount that you can sell it for, but if you are willing to accept your intrinsic values as fluctuating with those conditions, you might just as well call that intrinsic as anything else, I should think.

Senator GLASS. I am a countryman and my neighbor, another countryman, knowing not any more about it than I, would suggest to me in 1929 that if I would make a marginal purchase of American Can—

Mr. KENT (interposing). What was it, 143?

Senator GLASS. You will have to ask my Bishop about that. I do not know. [Uproarious laughter.] Now, to get back to the point, were he to suggest to me that buy on margin a thousand dollars of American Can; upon the supposition that I had a thousand dollars, do I know anything about the intrinsic value of that property?

Mr. KENT. Not if you were willing to say, yes; you would like to buy it, without looking it up, but you could have looked up—

Senator GLASS (interposing). Well, how many do you think look it up?

Mr. KENT. Well, whose fault is that?

Senator GLASS. Oh, well; now.

Mr. KENT. There are opportunities existing to look it up.

Senator GLASS. I give it up.

Senator FLETCHER. Mr. Kent, may I ask you if this whole \$67,000,-000,000 of stock issues, of capital issues as you call it—

Mr. KENT. Yes.

Senator FLETCHER. Was unloaded on the public in the country?

Mr. KENT. Why, I would not say unloaded on the public, because that is more or less of a wrong way to put it. You have got to take things as they are.

Senator FLETCHER. Well, distributed to the public.

Mr. KENT. What happens is this: An industry, for instance, wants funds. They study their capital structure. They study their plant. They study their needs for expansion, and they see that if they can obtain a million dollars, we will say, that they can utilize it to increase their business on what seems a sound basis in connection with the price commodity level at the time and the demand for goods, they therefore make an arrangement with the banker under which the banker sells for them, we will say, a million dollars of bonds or preferred stocks or whatever you choose, and the banker advertises that issue and he also ordinarily gives a picture of the business, shows the statement, shows what the earnings have been over a period of years back, and so forth.

Now if that security appeals to those who study those advertisements and it is sound, based on the statement of the company, people buy it. That is not unloading them on anybody. It is telling them the facts, and then they can use their own judgment. Every individual in this world has got to use his own judgment in the things that he does himself. We can not change that.

Senator FLETCHER. I know that, but is that the method by which this \$67,000,000,000 of securities was distributed? Is that the method, usually through the banks, and the banks recommend it?

Mr. KENT. Not always through the banks. Sometimes it is done through stock exchange houses, who are really bankers in a sense.

Senator FLETCHER. The result of all that is how much loss to the public? Didn't that withdraw cash from people's homes and their possession to an enormous extent? Was not that partly the cause of this depression, the unloading of these securities of \$67,000,000,000 on the public, all of which have been pretty nearly lost?

Mr. KENT. Not necessarily. If a person had to sell to-day, stock bought in 1929, there would be a loss. If they carry that stock, and they are able to, and it is in a sound company and a good business, there is no necessity why it may be a loss.

Senator FLETCHER. All right.

Mr. KENT. The market goes up and down. That is based largely upon the movement of business, and of commodity prices. For instance, take commodity prices as they are to-day; we can probably anticipate that the time is going to come some day when there will be a little motion in those commodity prices, that is a little rising motion. Why? Because goods are desired by the people and the retailers who ordinarily carry those goods will find that their shelves are bare. They put an order upon the wholesaler. The wholesaler orders from the manufacturer. The manufacturer orders from the raw-material man. And so it goes on back to the beginning and there becomes a little movement in commodity prices, a little demand.

Then as others who manufacture see that that demand is causing a little rise in prices they will begin to buy more of the goods which they require for processing than they have been buying and that will add to and accelerate somewhat the movement of the commodity prices of this and that and the other thing. As that gathers force from a multitude of operations of that kind, then the desire to buy early goes from those who are manufacturing through the wholesalers, and the retailers begin to load up their shelves beyond what they actually require at the moment, for fear that they are going to have to pay higher prices if they wait.

And so you have a moving commodity price level that gets higher and higher and higher, and the banks are obliged to loan more money in order to allow a client to process the same amount of goods, because the prices of goods are higher, and so it goes on up.

Senator FLETCHER. I understand that.

Mr. KENT. Now, the profits of nearly everybody then become greater because if they buy on a rising commodity price basis some time before they can sell, they must have a wider profit, because of the movement of the commodity price.

That means that taxes that the Government gets are higher on the same base of taxation and the Government gets more money than it has been getting without changing its base of taxation, and the Government then begins to spend that money and the Government develops then a budget that reaches a point where, when the commodity prices turn and go the other way and profits are not as great and its income falls off, it has a momentum of expenditure that it can not stop without a great deal of difficulty.

That is true in this whole world at the moment, and that is the thing that we are trying to get out from under.

The business man and the individual from all over the world have been cutting their expenditures because they have had to. Governments have not done it, not because they have not wanted to always, but because it is tremendously difficult because of the momentum of expenditures that have come about on the upward turn, and that is one thing that we all have to learn. If governments will learn to stop their expenditures as commodity prices reach a normal level and begin to go above it, then you will find it will be very helpful to this world in preventing such things as happened in 1929.

Senator FLETCHER. How does that all apply to agricultural products? You are speaking about commodity prices.

Mr. KENT. The agricultural policy?

Senator FLETCHER. Agricultural products.

Mr. KENT. Well, agricultural products have fallen more than others. As I recall it, from 1930 to 1931 in December all commodity prices, the average fell 15 per cent. Of that the agricultural prices fell 22 per cent, and the nonagricultural prices 10 per cent. It has made a very difficult situation for the agriculturists, and I think it would interest you very much if you carried it into the thought of what these foreign governments have to do in order to pay off their loans. Their situation is very much more difficult than is the situation of those in this country, for instance, who had to borrow.

Now we know the difficulties that New York, Chicago, and other cities are having in meeting their obligations, but they are in dollars, and those obligations are in the money that they receive from taxes. But you take the countries of South America, for instance: They have obligations in dollars. The income that they receive is in their own monies, and how do they receive dollars? They obtain dollars through the exports of certain agricultural commodities in large proportion.

So that the Peruvian Government, for instance, depended upon the exports of cotton and sugar and of copper and of oil for the foreign exchange that they used to meet their debt charges. The prices of those commodities have gone down tremendously. Consequently Peru does not receive at the moment the number of units in dollars that it did receive before the commodity price level fell. That has been a tremendous loss to Peru.

Senator BROOKHART. Doesn't that mean that we ought to change the gold standard so as to give them a square deal?

Mr. KENT. Oh, no; the gold standard has nothing to do with it. There is no motion in the gold standard, absolutely no motion in the gold standard. The gold standard is merely a measure of commodities, particularly as between each other.

The CHAIRMAN. May I ask just a few questions on this intrinsic value?

Mr. KENT. Yes.

The CHAIRMAN. I notice you did not mention replacement cost as one of the bases. Do you consider that important or do you not?

Mr. KENT. Intrinsic value—I do not think so, because it must be a fluctuating value based upon commodity prices, together with an earning capacity of the corporations which may have issued securities.

The CHAIRMAN. But I notice when apartment houses cost more to put up they can borrow more money than when they can be built cheaper.

Mr. KENT. Yes, but of course you have to bear in mind that when men are operating on any particular commodity price base that is the thing they see. They have the present sense of the moment, but they have no positive sense of the future. They have a feeling, maybe, that commodity prices may be going up or may be going down, but they have no certainty. They have no positive knowledge about it.

The CHAIRMAN. No, but is it not a fact that many commodity prices on much of the building, that the replacement cost of that depends on the wage scale and that as that goes up or down the values of the whole thing change?

Mr. KENT. Well, the wage scale ordinarily in the production of the average manufacture, I think, is 27 per cent of the total cost.

The CHAIRMAN. And you will agree with me, pretty nearly a hundred per cent on farm products?

Mr. KENT. On farm products?

The CHAIRMAN. Yes; the labor that goes into it.

Mr. KENT. The farm products proposition is a very difficult one, of course.

The CHAIRMAN. But I notice this; at the moment the wages get up, the railroads begin to pay more for their ties and their rails, as well as having a higher pay roll.

Mr. KENT. The rails have been the same price for many years.

The CHAIRMAN. In our region they are not. They were cheaper at one time than they are now.

Mr. KENT. They are not since the depression.

The CHAIRMAN. No; it seems to be a controlled commodity that does not respond to something else.

Mr. KENT. It was based on long-term arrangements for price that covered labor on a certain basis, of course, and raw materials and everything of that character.

Senator BROOKHART. It is \$43 just the same as it was in the high war period?

Mr. KENT. Yes.

The CHAIRMAN. I am not sure that I understand you on the \$67,000,000.

Mr. KENT. Yes. That is the market value of the domestic bonds, the foreign bonds, and the stocks on the stock exchange at the moment.

The CHAIRMAN. How much of those are marketed annually in this country?

Mr. KENT. I gave those figures. They showed 2,300,000,000 in five years up to 1924, when it ran up to 4,600,000,000, and in 1929 it was 8,600,000,000, and it dropped off in 1930 to a less sum. I have those figures here. It was very much less than in 1931.

The CHAIRMAN. If they are in your statement I do not care to have you repeat them. I was simply trying to figure out what part of the national earning goes into those investments.

Mr. KENT. I should say pretty close to 7 per cent, if you figure national earnings on the basis that has been worked out. They were figured to be 71,000,000,000 in 1930. They were 83,000,000,000 in

1929. It is felt that it will show something very close to 60,000,000 in 1931. But the figures are not available yet in their entirety. Of course, you can see the taxation against that is very terrible. In 1930 the taxation in the United States was 13,000,000, including that needed by the Federal Government, the States and municipalities, and that represented a very high proportion of the national income.

When that happens what really occurs is that those supposed to be wealthy pay with dollars and the poor man pays with his job. That is the result of excessive taxation. The poor man does not see that he is paying with his job when you have excessive taxation, but it has developed so clearly in Great Britain, Germany, Australia, and other countries, that looking back over their picture you can see actually that that has happened.

The CHAIRMAN. Now then, on taxation, is not the tax dollar something that also responds to the price level?

Mr. KENT. Yes; in so far as the receipts of Government change. They fell with the commodity price level.

The CHAIRMAN. And only part of the tax is due to liberal expenditures?

Mr. KENT. No; government goes on and expends the same amount, and then it raises taxes in order to get it. Government does not hold the same base of taxation when you get a fall in commodity prices. If it did, it would not be so difficult to pay.

The CHAIRMAN. If the Government must pay more than that when we have a lower wage scale, it means an increased tax, even though you do not have any more clerks?

Mr. KENT. Well, it works this way: If you hold your base of taxation the same—

The CHAIRMAN (interposing). You can not do that unless you hold the salaries and the wages the same, can you?

Mr. KENT. No.

The CHAIRMAN. And commodity prices the same?

Mr. KENT. Of course, but they do not move in conjunction or proportionately. They move in this and that and the other spot. That is quite necessary, because of the dispersion of prices. A price level is not a movement of the same percentage in proportion to every commodity. If the commodities cross each other up and down based on supply and demand, there is a great dispersion.

The CHAIRMAN. For instance, the national earnings during the period from 1914 up to 1918 had an enormous rise compared to other years?

Mr. KENT. Yes.

The CHAIRMAN. And that national income was largely the result of an inflation of commodity prices and higher wages, was it not?

Mr. KENT. Yes; because the majority—

The CHAIRMAN (interposing). Therefore, it was a correct measure?

Mr. KENT. The majority buy before they sell. If commodity prices are rising between the time that they buy and the time that they sell, their margin of profit is wider. That is what causes the greater profit, and on the same basis of taxation it means that Government gets more.

The CHAIRMAN. To take an illustration close to home: A school-teacher used to teach school for twenty-five to thirty-five dollars a

month. Since the higher wage scale became effective, she receives a hundred dollars a month, country teaching. That school tax is bound to be three or four times as high, even though you have the same teacher and no additional schools.

Mr. KENT. Of course.

The CHAIRMAN. And we are told it is extravagance.

Mr. KENT. That is on the other side of it.

The CHAIRMAN. Yes; but it is one side of it.

Mr. KENT. It is a very important side of it.

The CHAIRMAN. Yes. In other words, it is not all extravagance. Much of it is part of the changing conditions under which we are operating.

Mr. KENT. Oh, that is true. That is true. And it is very difficult to make adjustments that can be considered fair, because everything does not move proportionately the same.

The CHAIRMAN. After all, is not the main question whether we are to be on a higher level or on a lower level?

Mr. KENT. No; we must be on a fluctuating level.

The CHAIRMAN. How is that?

Mr. KENT. There must be a situation where we are on a fluctuating level. What we must strive to do and what I hope we can do in this country is to find a means to determine more closely to the current moment the progress and the relation between production and consumption. For instance, November, 1929, was really the first time we knew that the business of those engaged in many commodities had begun to fall off in May, 1929. If we had been aware of that very promptly in May it would have been possible for those whose business was getting in bad shape to have protected themselves a little better. That is what we are striving to do through the National Industrial Conference Board. We are trying to bring closer to the present moment knowledge of what is happening and when this, that, and the other industry is going down. Then when we have that we are going to try to determine the cause and control it.

There are many things that enter into changing business. New inventions, changes in the habits and customs of people, new discoveries or conditions that show there is going to be a turn in the whole commodity price level. That is going to take time. When we get that character of information, except as waves of extravagance go over the people of the world—and they seem to go in spite of us—it would then mean that we would keep the movement lower at the high part and higher at the lower part of the curve, which would make less hardship for the people. That, of course, is what we are striving for.

The CHAIRMAN. In other words, a more uniform level on which to do business?

Mr. KENT. Yes.

The CHAIRMAN. Less subject to fluctuation?

Mr. KENT. Yes. But there must be fluctuation, because the human mind works that way, and do not think, Senator Brookhart, that there is any motor or any self-starter or any mechanical brain in a bar of gold. Gold is inanimate.

Senator BROOKHART. And it fluctuates in intrinsic value the same as anything else, and when it goes up everything else goes down because of the deflation?

Mr. KENT. But that is not the reason; that has not been the reason during the depression. Gold has nothing to do with this depression, in my opinion.

Senator BROOKHART. Let me ask you another question: I am a subscriber for your National Industrial Conference Board, and I think it is very valuable. Your latest estimate shows that our national income last year in dollars was \$57,000,000,000; that is 1931.

Mr. KENT. 1930 was seventy-one billion.

Senator BROOKHART. Yes; seventy-one billion for 1930, but fifty-seven billion for 1931.

Mr. KENT. Well, yes.

Senator BROOKHART. That would be \$2,210 for each average family of five. It seems to me that would be enough to keep things prosperous if it were distributed.

Mr. KENT. That is enough to keep a vast amount of production going on, but this is a tremendous world, and the number of units of production that are necessary to provide during ordinary times that are not purchased during times like this is so great that it means a great fall in the utilization of the productive capacity of the world.

Senator BROOKHART. If a few big corporations get that income and discharge their men to protect their profits, I can see where that would bring on trouble and remove buying power and all of that. But if this \$2,210 were distributed, everybody would have something to buy with and prosperity would go on.

Mr. KENT. You can only distribute money effectively when something is given in return for it, and the problem of developing a situation of that kind is very hard.

Senator BROOKHART. You are familiar with the cooperative organizations in various countries?

Mr. KENT. Yes.

Senator BROOKHART. They do not depend on that. They fix the wage of capital to start with right away, just as they do for the men. The English cooperatives pay about 3½ per cent, and they are more prosperous than the competitive business in England and have gone right along even ever since the war.

Mr. KENT. Well, of course, they carry things that are, you might call, the commodities of life that people are able to buy from the dole.

Senator BROOKHART. Yes; but so do other people. They have to buy it just the same as they do in any other country, for that matter.

Mr. KENT. Yes; certain things.

Senator BROOKHART. And they have had no bank failures over there with their cooperative banks.

Mr. KENT. That is a very different institution from ours. They have a certain special purpose.

Senator BROOKHART. They have a couple of hundred factories doing everything in human civilization. They have not had any failures, going right along, because they fixed the wage of capital all the time. So is that not a sounder system of business than this of ours?

Mr. KENT. I did not quite get that. I am sorry.

Senator BROOKHART. I say, is that not a sounder system of business than ours?

Mr. KENT. No; that only applies to some certain character of business.

Senator BROOKHART. You do not understand it then, because I could not find anything that anybody else was doing in England that they were not doing. They were into everything, and business everywhere, all around the world.

Here is another thing: If 3 per cent is all we produce in this country, if that is all the wealth production we have—

Mr. KENT (interposing). That is an increase.

Senator BROOKHART. I understand; the wealth increase—if that is all we have, if we organize corporations and send them out in banks or railroads or anything else to fight for 5 $\frac{3}{4}$ or 10 or 40 or 100 per cent, are we not in a state of economic warfare that is going to produce these ups and downs all the time?

Mr. KENT. But we do not do that.

Senator BROOKHART. We do not? Why, we gave the railroads a right to fight for 5 $\frac{3}{4}$ per cent by law, and they get that \$7,000,000,000 watered value besides.

Mr. KENT. Yes; but you went on up to 100 per cent.

Senator BROOKHART. The Standard Oil Co. got as much as 600 per cent at one time.

Mr. KENT. In a turnover you can get most any per cent, but that has nothing to do with the interest on money.

Senator BROOKHART. There is only 3 per cent left for distribution. That is all we got finally over our living and operating expenses and wage, and if somebody is dipping out to 100 per cent, why, somebody else has got to lose. That is all there is about it. And that is figuring everything to capital alone, not to anything else. Capital is getting all the wealth increase on that 3 per cent basis.

So, are we not organized on an unsound basis to start with, that is going to continue to produce these inflations and deflations and requiring first one psychology and then another to get along?

Mr. KENT. That one psychology and another comes from actual operations in commodities, based on supply and demand and the opinion of men as to what that is going to be.

The CHAIRMAN. I wanted to ask—your statement of 27 per cent of wages applies to what?

Mr. KENT. Twenty-seven per cent of the cost of a certain block of production goes into wages.

The CHAIRMAN. I know the statement has been made that in the construction of highways only 15 per cent goes into wages. The cement that is used is mostly wage cost, is it not? The steel that is used is largely wage. The machinery that goes into it is largely wage. The transportation that goes into it is largely wage. Would not the actual wage, if you followed it clear down, be 90 per cent?

Mr. KENT. It might seem so, as we think about it; but actually, when you get all the figures together, they came to 27 per cent. I will try and see if I can get those figures. I think I can find them for you.

The CHAIRMAN. It is either one thing or another. It is either wages or earnings on capital; is it not?

Mr. KENT. It is wages and raw materials.

The CHAIRMAN. But raw materials are wages.

Mr. KENT. Oh, you are figuring raw materials in wages?

The CHAIRMAN. Well, it takes labor to produce raw material as well as finished products.

Mr. KENT. Yes. I would separate them. There are wages and raw materials and distribution expenses.

The CHAIRMAN. In other words, you get the 27 per cent by cutting off at a certain place instead of following it clear through?

Mr. KENT. Yes; I was talking about direct wages.

The CHAIRMAN. That part was the basis of my remark that most values were a reflection of the wage scale and the labor costs, and that replacement values are often largely a question of what the wages are. Buildings cost one price at \$3 a day and another one at \$6 a day.

Mr. KENT. I will try and remember to send you the report of the National Industrial Conference Board that showed the percentage of cost that wages take.

The CHAIRMAN. But this much we are agreed on; that it did not go the whole way through?

Mr. KENT. Oh, no.

The CHAIRMAN. That is all I wanted.

Senator BROOKHART. I will give you some figures on that the whole way through. In 1926 I believe was the year—it was about that—manufactured products had a total of \$60,000,000. The total wages paid, all wages, all labor, all producing, all raw materials, and everything else, was \$11,000,000 out of sixty.

The CHAIRMAN. Then the rest was profit.

Senator BROOKHART. The rest was profit, yes; and doubling up of cost of raw material.

Senator FLETCHER (presiding). Have you finished with Mr. Kent.

Senator GLASS. I do not see that I expedited these proceedings by leaving the room for a half an hour.

Senator FLETCHER (presiding). We are much obliged to you. I believe that is all now.

Mr. KENT. Thank you, gentlemen. I appreciated the opportunity to talk with you.

(Thereafter Mr. Kent submitted the following letter, which was ordered to be made a part of the record:)

NEW YORK, March 31, 1932.

HON. PETER NORBECK,

*Chairman Committee on Banking and Currency,
United States Senate, Washington, D. C.*

DEAR SENATOR NORBECK: Several times at the hearing yesterday it was in my mind to state specifically in answer to some of Senator Glass's questions that my reference to stock exchange operations were confined entirely to the ordinary regular and sound dealings that represent its normal business.

There is in my opinion a vast difference between such operations and what is called "stock gambling," and I hold no brief for the latter. It does seem to me most unfortunate that because there are those who may engage in stock gambling that a reputable, sound, and much-needed financial process should be so unfairly criticized as is the New York Stock Exchange.

As questions came back at me quickly the several times when I was about to express my disapproval of so-called stock gambling, as separated from the regular stock exchange business, I did not have an opportunity to clarify my opinion before the committee in connection with this phase of the matter.

It is my firm belief that the officers responsible for the running of the New York Stock Exchange exercise to the highest degree intelligence and integrity in the control of stock exchange operations. It is inconceivable to me that the exchange could be in better hands from the standpoint of business safety and good citizenship. Further I feel very sure that such abuses as occur are in tremendous percentage due to the acts of individuals who are not members of, nor associated directly with, the stock exchange itself.

It really seems most unfortunate that the stock exchange market which is so necessary to our financial structure is so consistently ignored in connection with its real purpose and uses and that the accent is placed upon the opportunity offered to gamble which is inherent in almost all the activities of mankind.

Whether you would consider it orderly to file this letter with the testimony I do not know, but in any event I was anxious to have you and Senator Glass, to whom I am sending a copy of this letter, realize through positive statement that my expressions of approval of the upholding of a market for securities upon the stock exchange had reference to the legitimate, normal, and ordinary business that is carried on, and did not refer to mere stock gambling any more than my reference to the businesses of banking, industry, or trade referred to the abuses of a similar character which are possible to them as well as to every form of business endeavor.

Please allow me to accept this opportunity to express my appreciation of the courtesy extended me by you and the members of the Banking and Currency Committee of the United States Senate before whom I had the honor to appear yesterday.

Sincerely yours,

FRED I. KENT.

Senator FLETCHER (presiding). Mr. P. D. Houston.

STATEMENT OF P. D. HOUSTON, CHAIRMAN OF THE BOARD OF THE AMERICAN NATIONAL BANK, NASHVILLE, TENN.

Senator FLETCHER. (presiding). Mr. Houston, you may state your name and address and business connections for the record, please.

Mr. HOUSTON. P. D. Houston; chairman of the board of the American National Bank, Nashville, Tenn.

Senator FLETCHER. Mr. Houston, you have examined this bill, have you, S. 4115?

Mr. HOUSTON. I have read it several times.

Senator FLETCHER. Just tell us what you think about it.

Mr. HOUSTON. I am going to be very brief with you, because I think you must be more tired than I am, and I have been here all day.

This bill under normal conditions would not be especially objectionable; but at this time, when the entire country is emerging from the greatest depression and resultant deflation in history, it would be to the best interest of recovery to normalcy not to require such drastic changes in banking operations. Confidence in banks and business is more composed since the passage and functioning of the Reconstruction Finance Corporation, because in my opinion it will assist in enabling all solvent banks to meet their obligations. Banks are simply public institutions and must be controlled under well-defined laws governing their operation, but not to the extent that the human element will be crowded out or be too much restricted. Banking as well as credit is based largely upon confidence, and psychology plays an important part. To make such radical changes in bank operations just at this time would in my opinion retard recovery to normalcy of banking and business.

In section 8, which deals with collateral loans by member banks, this bill in my opinion discriminates against collateral loans, the proceeds of which not infrequently find their way into commercial

transactions. I do not think that any of us will disagree that credit once issued can not be controlled. A bank is always just as good as its management. A commercial banker to-day recognizes his responsibility and endeavors to the best of his ability to keep his bank in such condition as he can always find a resting place in the Federal reserve.

Whenever he invests largely in collateral loans, to that extent he impairs his ability to take care of his demands from time to time as his customers make calls. Now, normally a bank can operate on a very small cash position, but in times such as we passed through during the past several months a bank is compelled to be in a strong position in order to maintain the confidence of the people with whom it is privileged to do business.

Senator GLASS. Were you here yesterday?

Mr. HOUSTON. Only after 4 o'clock. I heard just about 10 minutes of the Federal reserve governor's report.

Senator GLASS. You did not hear the board's proposed amendment, unanimously approved by the board, to section 3 of the bill?

Mr. HOUSTON. I did not, Senator.

I am going to pass on to section 8, which deals with the Federal Reserve Board's power to control loans to member banks. This section would be most disastrous to the majority of banks, as their funds could not be profitably invested or loaned on paper eligible for discount by the Federal reserve bank. The amount or percentage of eligible paper in portfolios of banks has steadily declined for several years, due to the issuance of preferred stocks, bonds, and debentures by commercial and industrial corporations on the accumulation of earnings over a long period of prosperous times, rendering it unnecessary to use bank credit. These corporations were the largest lenders to brokers on the stock-exchange collateral during the recent past. To restrict such loans by such a severe penalty would at least be very unjust and would also bring about a liquidation of security loans that would cause further deflation and lowering of commodity prices. Many, if not a majority, of the banks have more than their capital and surplus invested in collateral loans at this time.

Section 9 deals with the limitation of member banks' loans to affiliates, and the ownership of the capital stock, bonds, or other obligations of an affiliate. This section practically does away with affiliated trust companies, security companies, and mortgage loan companies, as the provisions of this section would render it impossible to continue these operations profitably. I am familiar with institutions engaged in the mortgage loan business and having correspondent relations with large insurance companies, giving them an outlet for their loans, but which, for good reasons, have accumulated loans necessitating borrowing from the parent bank in excess of 10 per cent of the capital and surplus. In some instances the loans were held to accommodate the parent bank, but when not the case, the excess was for only a short time. Some insurance companies also give commitments in the form of acceptances, but their correspondents agreeing that on a certain date 30 days, 60 days, or 90 days hence that they will purchase a certain specified loan. Those obligations have always proven to be the most desirable and certain bank investments, because they are always taken up promptly as they mature. To exclude the collateral as set forth in this sec-

tion on loans would be unreasonable and not necessary to the safety of the bank or the affiliated institution.

Section 10 deals with the Federal open market committee and the Federal liquidation corporation. The present open-market policy of the Federal reserve banks has been successful so far as I have observed, and I do not believe the creation of an open market committee is necessary or in justice to the autonomy of the Federal reserve bank of each district.

Section 10 also provides for the creation of a Federal liquidating corporation and defines the organization, its functions, and so forth. The provision with respect to member banks' contribution to capital stock seems to be too great a percentage of the total capital, and restricts the return on same to 6 per cent, to be paid out of 30 per cent on the net earnings of the corporation. It is not clear to me how there will be any profits except from interest accrued and collected on assets bought; and it is my observation that paper of defunct banks is more difficult to realize on than that of going institutions; and with a 6 per cent liquidating charge, some portion of the interest collected would be absorbed in expensive operation. Then, too, I have wondered why the 6 per cent paid to member banks was restricted to 30 per cent of net earnings, and what disposition would be made of the remaining 70 per cent. This provision entails a large responsibility on the governing board which will be an arm of the Federal Reserve Board, and it is my thought that this section is of such importance that it would be best stricken from this Act and introduced as a separate and distinct measure.

Section 11 deals with the rate and the limitation on member banks borrowing on 15-day bills payable. This section is consistent with the basic purpose of this act, to curb speculation by the aid of Federal reserve credit. The penalty prescribed on 15-day borrowing by member banks will prove more expensive to the United States Government in its financing than it will to member banks, as the rate of interest charged by member banks can be and will be adjusted to the cost of credit. This provision should, in the general interest, be omitted.

Section 13 deals with new reserve requirements, sale of funds, and so on. This section defines demand and time deposits and provides an increase in reserves on time deposits to equal those on demand deposits. Reserves are primarily for providing the Federal reserve banks with loanable funds and gold to support Federal reserve notes; 10 or 13 per cent of deposits in cash will not pay 100 per cent deposit liability. The increasing of the reserve on time deposits will reduce the loanable funds of member banks and will be most hurtful in the agricultural districts, as well as impose an added burden upon member banks. In my own bank this provision would increase the reserve approximately \$1,000,000. It would, therefore, not only deprive us of revenue or income on \$1,000,000, but it would reduce our loaning funds to that extent.

Senator GLASS. What are the deposits of your bank?

Mr. HOUSTON. Our deposits are \$40,000,000.

Gentlemen, since I have been here to-day, I have heard so much of this discussion that I do not know whether I am going or coming, but I really feel that this matter is one that ought to be considered purely from a practical standpoint, and I know that you

gentlemen want to consider it for the best interests of the whole country. You do not want to consider it from the standpoint of any class; not for the banks, but for the business people as a whole. I, frankly, do not feel that the laws of this country make a dishonest man honest. I will admit that the laws do curb a man and keep him within the straight and narrow road to some extent, but any business is just as good as its management, and if you have a bank that is not officered by men who appreciate their obligation and the trust that is reposed in them, you are not going to have a sound institution no matter what kind of laws you put around them.

The Federal reserve banks have done a wonderful thing for the business of this country. I have had pretty intimate contact with the Federal Reserve Board. I have been a member of the advisory council. I have been in pretty close touch with the operations of the bank of our district since its organization, and I do know that while they have their limitations prescribed in the act, the management of our bank—and I think I can say that pretty well of the banks over the country—has tried to consider the interests of the public and has tried to make the law apply as the exigencies of the occasion demanded. I have heard it mentioned here to-day that probably the Federal Reserve Board and other Government officials in charge of the conduct or supervision of banks have been too lax. Now, it is mighty easy for us to criticize people for things that are past. I believe that the Federal Reserve Board and I believe that the comptroller's office have tried to serve the best interests of this country at all times. I suspect they would admit now they made many mistakes, but the problem that you have before you to-day is passing legislation that will strengthen the business structure of this country of ours; and I will say as a banker that I welcome any legislation that will not impose a hardship, that will not require a change of policy which would further aggravate the conditions that obtain to-day.

I want to be a little bit more personal. I am chairman of a board of a bank where, during the period of November 15 or 16 or something like that date in 1930, the firm of Caldwell & Co., located in my town, became involved. We tried to pass it on to the public by degrees. We first met around the table, not in night sessions—this was daytime—and we decided that rather than to break the news very abruptly, we would advise the public that the bankers' committee had taken charge of Caldwell & Co. The bankers' committee was appointed and did take charge of Caldwell & Co., but it was inevitable that the institution was not able to go along, resulting in embarrassment to the First National Bank, which was closely allied with Caldwell & Co.

They began to suffer a loss of deposits. Our institution furnished them \$1,500,000 the first day after the closing of Caldwell & Co., \$500,000 another time, and \$1,000,000 another time. Finally we had furnished approximately \$4,000,000 to that institution. In addition, it aided them in borrowing money from correspondents of ours until they had involved themselves to the extent of \$15,000,000 in about four or five days.

The CHAIRMAN. Then what?

Mr. HOUSTON. Our institution, then, had to commence to take them over; not from choice, but, gentlemen, as I said in my remarks a while ago, it is very seldom that a bank which becomes so depleted in resources that it has to close its doors finds its remaining paper of such character and kind that one can put a value upon it with anything like a degree of certainty.

Now, after we took over that institution, within 75 days we cleared the liability of \$15,000,000. We did it mainly from the assets of the American National Bank, because we were prepared for just what came. We had paper that was of the eligible character and paper that was self-liquidating. But the time has passed and we have had a lot of changes in the past six or eight months. Since the turn of the year 1931 there has been the most drastic decline in values of all kinds, not only in the stocks and bonds, but real estate, commodity prices, and everything has shown such a decline that we have never been able to determine whether we have reached the bottom even now. That being the case, it has been the biggest task that a banker has ever had in my time to determine just what was for the best interests of his community and his client; whether or not to force him on the market, sell him out when the banker had the feeling that this was not a normal market. It was brought about by a fancied situation. The security appeared, from analysis that was made, worth far more than the then market value. So a banker has a difficult problem to determine whether he shall sell out and thereby further aggravate the conditions.

In our particular case we have had this difficulty in commodity prices. We have had declines in security prices. We have had Bolshevik tendency. We have had people that were broke due to overspeculation.

Senator BROOKHART. The Bolsheviks are the only ones that have not had any difficulty. [Laughter.]

Mr. HOUSTON. They were down already.

Senator BROOKHART. They have gone up faster than we have gone down.

Mr. HOUSTON. Well, that might not have been the proper term. But there are a lot of people that we want to sympathize with, people that were financially down, and they seemed to get pleasure out of involving others. There have been all kinds of rumors throughout our section of the State. We have had a good many bank failures in Tennessee; not so many as in the majority of other States, but we have had far too many.

The CHAIRMAN. May I ask there: Is the fundamental thing a decline in the earnings of people and the shrinkage in values?

Mr. HOUSTON. No. The main trouble, Senator, with the people in our section is that they forgot themselves and went wild on buying something without regard to whether it was worth the price they were paying for it.

The CHAIRMAN. They represent the city people or the country people?

Mr. HOUSTON. Everybody; country people, city people, preachers, doctors. [Laughter.]

The CHAIRMAN. The presidents of the American Bankers' Association made out, apparently, a very strong case here against the farmers, because the price of farm land had doubled during

a certain period. Before we got through with him he admitted that what he said about the farmer's product applied to all other commodities.

Mr. HOUSTON. I am a farmer. You are talking my language now.

The CHAIRMAN. But you had that decline in earnings?

Mr. HOUSTON. We surely did have it.

The CHAIRMAN. And you say it cut no figure?

Mr. HOUSTON. The decline of the farmer's earnings?

The CHAIRMAN. Yes.

Mr. HOUSTON. Why, certainly.

The CHAIRMAN. I thought you were basing it all on extravagance.

Mr. HOUSTON. Not altogether.

The CHAIRMAN. You can not say whether the fundamental thing was the decline of earnings and the shrinkage in property values?

Mr. HOUSTON. I am talking about this banking situation now. I was not talking about general business.

The CHAIRMAN. No; but is not the banking situation quite responsive to the business conditions of the country?

Mr. HOUSTON. Absolutely; but it depends upon purchasing power; and in the Southland, Senator, agriculture is our principal source of new wealth.

The CHAIRMAN. Then we can understand your banking situation without any further explanation.

Mr. HOUSTON. I understand it, too; but it is not altogether agriculture. It is overspeculation. It is exactly what you gentlemen have in your mind to-day that you want to curb.

Senator GLASS. You do not mean to say any preachers have speculated?

Mr. HOUSTON. Absolutely. Methodist preachers, too, and one bishop. [Laughter.] He talks about it in the pulpit.

Senator GLASS. I am horrified.

Mr. HOUSTON. Yes, sir. A good fellow, too.

Senator BROOKHART. I was at Louisville when the National Bank of Kentucky failed. That was connected with this Caldwell enterprise, was it not?

Mr. HOUSTON. Yes. As I was staying a moment ago, I am in favor of any legislation that you gentlemen can devise that will improve the business structure and the banking structure of this country. However, I do not think that it would be wise to force my bank, for instance, to restrict its security account to the amount which would be permitted under this act. We have \$3,000,000 capital and \$3,000,000 surplus, and, as I figured it out, we could carry only \$1,225,000 of securities. We could not buy of any one issue more than 10 per cent of the amount of that issue.

Senator BULKLEY. That is the same trouble we have had right along. The wording is very unfortunate. It does not mean at all what you said.

Mr. HOUSTON. I have it in my own digest.

The CHAIRMAN. We plead guilty to some things.

Senator BULKLEY. That language is quite bad. You are not to be criticized for misunderstanding that. It just does not mean that at all.

The CHAIRMAN. We did not intend it to mean what it seemed to mean.

Senator BULKLEY. There is no such meaning.

The CHAIRMAN. We did not mean to put such restrictions on as many bankers have read into it on a reading of the bill.

Mr. HOUSTON. I can not believe that you Senators would do that, because you have got to consider this from a practical standpoint. Now, as to whether or not you make this retroactive. As to the future, that would be different. But when anything is hanging over it is just like the Farm Board buying up wheat. That wheat is known to the consuming public and it is going to continue to have an influence upon the markets.

Senator GLASS. You are a farmer?

Mr. HOUSTON. Certainly.

Senator GLASS. Would not you regard yourself as impious to undertake to criticize the Farm Board in its surplus?

Mr. HOUSTON. No, sir. I am the treasurer of the Farm Loan—Federal Farm—I won't try to say it; some kind of an association. [Laughter.]

Senator GLASS. You do not want the banks to be managed like that do you?

Mr. HOUSTON. No.

Senator GLASS. You know what you are in the bank, do you not?

Mr. HOUSTON. Yes. [Laughter.]

The CHAIRMAN. May I ask: You stated that your main industry in Tennessee is agriculture?

Mr. HOUSTON. That is right.

The CHAIRMAN. Could you give us some figures of the value of your crops for a series of years?

Mr. HOUSTON. I could not do it, Senator. I am sorry.

The CHAIRMAN. Would you be willing to look that up and add it to your remarks?

Mr. HOUSTON. Surely. I can tell you something about one crop.

The CHAIRMAN. Let me ask you this: Have you a State census in 1925 of your State?

Mr. HOUSTON. A State census?

The CHAIRMAN. Yes.

Mr. HOUSTON. Do they have that anywhere else?

The CHAIRMAN. Yes; they do in most States. [Laughter.] In between the Federal census.

Mr. HOUSTON. We have everything anybody else has.

The CHAIRMAN. In giving the value of farm lands I would like to have you put two figures in: The Federal census, that shows the value of your farm land in 1920—

Mr. HOUSTON. You want the value of farm crops?

The CHAIRMAN. I want all of that, too; but with that I want your State census in 1925 of the value of farm land, giving the comparative strength of your farm lands, and you will see where your security went.

Senator BROOKHART. I think you will get all that in the agricultural yearbooks.

Mr. HOUSTON. You want me to furnish you the State census of 1925?

The CHAIRMAN. On land values in your State and the corresponding Federal figures in the Federal census of 1920; and I would like the value of your crops going along, say, from 1918 down, or

back as far as you like—the total value of the crops produced in your State.

Mr. HOUSTON. Do you want them classified?

The CHAIRMAN. Not necessarily.

Mr. HOUSTON. The value of crops from, say, 1920?

The CHAIRMAN. Well, say from 1915 down to the present day, as near as you can get it. I would like to get some comparison. You are going to find it very enlightening in your troubles.

Mr. HOUSTON. I will have the president of my farm association give you the information.

(Thereafter the witness submitted the following information for the use of the Committee:)

AMERICAN NATIONAL BANK,
Nashville, Tenn., April 11, 1932.

HON. PETER P. NORBECK,
Washington, D. C.

DEAR SENATOR NORBECK: You will recall while I was a witness at the hearing on the Glass bill the latter part of March, you asked that I furnish you with information as to the land values in Tennessee for 1920 and 1930, also the value of crops.

I made a request of Mr. J. F. Porter, president of the Tennessee Farm Bureau Federation, for this information and am to-day in receipt of his reply, and which I am pleased to inclose herewith.

I hope that this letter will give you at least some of the information you desired. However, if you will write me further, should there be any special matter which is not sufficiently included in Mr. Porter's letter, I will endeavor to procure same.

Awaiting your further favors, I am

Cordially yours,

P. D. HOUSTON.

TENNESSEE FARM BUREAU FEDERATION (INC.),
Columbia, Tenn., April 9, 1932.

Mr. P. D. HOUSTON,
Chairman Board of Directors, American National Bank,
Nashville, Tenn.

DEAR MR. HOUSTON: Answering your request for value of farm lands, etc., in Tennessee, I find, from the 1920 census, assessed land values to be \$1,024,970,894; in 1925, \$750,426,372; 1930, \$743,222,368.

This, as I understand, includes land and property outside incorporated towns.

I was unable to find in the census report the value of crops, but in the International Yearbook for 1925, I find that crops valued as follows:

Corn.....	\$56,284,000
Cotton.....	
Hay.....	23,518,000
Tobacco.....	16,045,000
Potatoes.....	4,040,000
Sweetpotatoes.....	4,536,000
Wheat.....	7,616,000
Oats.....	3,112,000

Just why cotton is not given I do not know. From the United States Yearbook of 1928 we have just found cotton for 1925 valued at \$39,905,460 and the seed at \$5,839,500, giving a grand total of farm crops in Tennessee for 1925 of \$160,805,900.

The census for 1930 gives 245,657 farms containing 18,003,241 acres.

I do not understand so heavy a slump in land values from 1920 to 1925 as compared with so small a decrease from 1925 to 1930.

If you wish further information, about the best place to find it in Nashville is at the State library.

Trusting this will be of some value to you, and with best wishes, I am,

Yours truly,

J. F. PORTER.

The CHAIRMAN. I did not intend to interrupt you. Have you completed your statement?

Mr. HOUSTON. I could talk to you all afternoon on this bill, but I have mentioned the matters that I think are of the most importance from a practical standpoint, and I am glad to be of any assistance I can.

The CHAIRMAN. We thank you for coming here. It is helpful to have things pointed out so we know how different provisions will affect different sections of the country and different interests. There has been no desire on the part of this committee to do this hastily. The proof of it is that a bill very similar to this was introduced by the Senator from Virginia nearly two years ago and it has been pending ever since, and this committee has conducted hearings for more than a year. I mean the subcommittee did. And then it was decided to conduct another hearing in the last two weeks, and we have been doing that so as to give everyone a chance. I think it has all been very helpful and I appreciate you coming here. Mr. Houston, I am very glad to have heard you.

Mr. HOUSTON. Thank you, sir.

The CHAIRMAN. That concludes the hearings.

(Whereupon, at 4.30 o'clock p. m., hearings on S. 4115 were concluded.)

(After the conclusion of this hearing, the committee granted permission to the representative of the California Bankers Association to submit a statement for the record, which is as follows:)

STATEMENT IN BEHALF OF COMMITTEE ON LEGISLATION AND TAXATION CALIFORNIA BANKERS ASSOCIATION

(Presented by Edward Elliott, vice president, Security-First National Bank of Los Angeles, Calif., chairman; W. R. Williams, vice president Bank of America National Trust & Savings Association, San Francisco, Calif., vice chairman)

WASHINGTON, D. C., April 4, 1932.

COMMITTEE ON BANKING AND CURRENCY,

United States Senate, Washington, D. C.

GENTLEMEN: In presenting this statement regarding Senate bill 4115 introduced in the Senate March 14 (calendar day March 17), 1932, we deem it desirable to take up in order the various provisions which we find objectionable, stating our reasons for the objections in each instance.

(1) Section 2 of the bill contains definitions of various types of affiliates.

A reading of the bill would seem to indicate a broad objection to the affiliate as a holding company, and a more specific objection to the affiliate that is an underwriter and dealer in securities. We do not wish to express any opposition to a policy which would lead to the eventual segregation of investment affiliates from banks, though we do feel that such a segregation should be carried out only over a period of years and not abruptly. While not opposing such segregation we respectfully suggest that more detailed information with respect to the relationship of banks and such investment affiliates would be helpful in determining final policy.

We do wish to object to so broad a definition of affiliates as would include, for example, a company organized solely for the purpose of holding the real estate used by the bank for banking premises, or one organized to perform the functions of a purchasing agent, or formed for the purpose of taking out of a bank delinquent real estate loans, or real estate acquired for debt, particularly agricultural properties.

In the last-named instance, better and more efficient management of these properties can be secured, while the bank is relieved of unsatisfactory assets.

There are a number of other affiliate institutions, some of them authorized by law, which might well be excluded from the breadth of the definition.

(2) Section 3 of the bill, page 3, beginning with line 9: In our view the idea underlying this section seems to be that it is possible to determine the purpose for which credit is to be used. We believe this idea is erroneous because of the varying character of rediscounts on the part of the individual bank and the impossibility of determining whether or not the bank is rediscounting for the purpose of making or carrying security loans. This section we believe should be omitted. In our judgment the Federal reserve authorities already have sufficient authorization to restrain undue stock speculation so far as that is effected by Federal reserve credit.

(3) Section 4 of the bill, page 4, lines 13 to 22: We believe the idea of preventing a bank from voting for a Federal reserve director when its stock is owned by other corporations to be unsound. Heretofore, ownership of stock in member banks has been permitted under conditions which, if this section becomes law, would arbitrarily and immediately deprive banks to which it is applicable, of any voice whatever in the selection of Federal reserve bank directors.

(4) Section 6 of the bill, page 5: We approve of proper examination of and reports on the part of all affiliates.

(5) Section 8 of the bill, page 9, beginning with line 15: It impresses us as wholly beyond the ability of the Federal Reserve Board to know the individual situation of the thousands of member banks sufficiently well to be able to determine for each one the percentage of its capital and surplus which, from time to time, may properly be represented by loans protected by collateral security. The exercise of such a far-reaching and detailed power of control over individual member banks must inevitably result in arbitrary and unjust administration. No bank whose loaning capacity would thus be subject to change upon 10 days' notice in the sole discretion of the Federal Reserve Board could possibly function with any degree of certainty. The utmost limit to which a regulatory agency, such as the Federal Reserve Board, should be permitted to go in such matters as this should be the adoption of general regulations which may be known and ascertainable by all institutions falling within the class to which such regulations apply.

(6) Section 9 of the bill, page 10: While we do not object to proper restrictions upon loans to and investments in their affiliates by banks, we do most particularly urge that any loan or contract of purchase and sale, when made to an affiliate for the purpose of taking real estate out of the bank, should under no conditions be regarded as an objectionable loan. There should be no prohibition against such transactions as they are always in the interest of the liquidity of the bank. Loans to other affiliates may be entirely proper. Certainly, affiliates nonfinancial in character, such as real-estate holding corporations, would be unable to secure their loans by the kind of collateral called for by this section.

(7) Section 10 of the bill, page 13, line 9, following: We do not believe that banks should be called upon to contribute anything to the stock of the liquidating corporation. At this particular time to require a bank to subscribe an amount equal to one-half of 1 per cent of its total net outstanding time and demand deposits on the last call date in the year 1931 would be a distinct hardship. It would mean a loss of earnings at a time when banks are sorely in need of them to take care of unusual losses inevitably incurred during any period of depression.

(8) Section 11 of the bill, page 25, line 4, following: The penalty of 1 per cent higher rediscount rate for member bank 15-day notes seems ill-advised, as this method of borrowing on the part of banks is the most convenient and economical, both for them and for the reserve banks. The further restrictions in the section upon security loans by member banks are so drastic as to seem ill-advised and extremely difficult, if not impossible, of enforcement.

(9) Section 13 of the bill, page 27, line 18 following: The tremendous increase in the reserves required by the provisions of this bill would create a great hardship for the banks through their lessened earning ability. Equally important would be the curtailment of credit necessitated by this great increase in reserves, as loans equal to the increase in reserves would have to be called. As an illustration of the effect of such additional reserve requirements, we cite the cases of two of the banks in California: For bank of America, National Trust & Savings Association, over the 5-year period, on the basis of present deposits, the increase would be over \$34,000,000, and for

Security First National Bank over \$22,000,000; for the first year the increase in reserves for Bank of America would be over \$8,000,000, and for Security First National about \$4,500,000.

Subdivisions (d), (f), and (g) of section 13, pages 30 and 31 of the bill, we think could not accomplish any good purpose. Under subdivision (d) it is practically impossible to determine whether the proceeds of such a transaction as indicated are to be used directly or indirectly for the purpose of making loans protected by collateral security. The mere difficulty of trying to determine would very much hamper legitimate activity on the part of the banks and doubtless the provision could be readily evaded. The dealing in Federal reserve balances instead of being improper as seems to be indicated by this bill, we regard as a very proper function in creating fluidity of reserve credit, and it is our understanding that the Federal Reserve Board already has set up machinery for securing all necessary information with respect to such transactions.

(10) Section 14 of the bill, page 33, lines 4 to 8: The revaluation by the Comptroller of the Currency of all real-estate loans at every examination would put an impossible burden upon the comptroller's office and an exorbitant charge upon banks. Moreover, there seems to be no sound reason why a real-estate loan made on an appraised basis for a period of three to five years should be adjusted every six months. The loan could not be called, as the bank, so far as the borrower is concerned, would be powerless to take any action until the loan was due. If there should happen to be a deflation in real-estate values meanwhile, a bank could under the application of this provision be rendered bankrupt, although its loans be substantially sound; the appraisal might not be twice the amount of the loan, although the value of the property remains adequate for safety.

Lines 17 to 20, page 33, contain the provision that investments in bank premises and unsecured loans whose eventual safety depends upon the value of real estate shall be counted as real estate loans. So far as investment in bank premises is concerned, it seems to us that a much better way of handling the matter would be to place a limit upon the amount which the bank may expend in bank premises. In our State, California, a bank may not invest more than one-half of its capital and surplus in bank premises without previous written consent of the superintendent of banks. Regarding unsecured loans, it would be utterly impossible to determine each individual case whether or not the loan depended for its ultimate payment upon the value of real estate, and in many cases where it could be so determined the loan, nevertheless, under no sound theory could be classed as a real estate loan. For example, take the case of an unsecured loan made to a rancher who owns his ranch free and clear, but who needs money for fertilizer, labor and material, fumigation of his trees, harvesting and marketing his crop, etc. Such loans for operative purposes are not real estate loans, and yet the banker may feel that eventual payment may be relied upon by the fact that the rancher owns his property free and unencumbered.

Page 33, line 20 following: The regulation of the investment of those time deposits, not invested in real estate, and their segregation for the benefit of time depositors, are such a departure that in our judgment they should not be undertaken at least without more careful prescription in the statute of the character of investments to be made, the extent of the segregation of these investments and perhaps also the establishment of a savings department with its own segregated capital.

In the California bank act there is such a segregation and allocation of capital and assets and a rigid prescription for the investment of savings deposits. While such a system is advantageous for the savings depositor in the event of the failure of a bank, the wisdom of introducing it into the national banking system may be seriously questioned.

The requirement on page 34, lines 4 to 9, that a bank shall be required to report the investments in which its time deposits are placed at a valuation which shall not exceed the market value at the time of the reports to the comptroller would, if acted upon by the comptroller at such times as these when there have been enormous fluctuations in the price of bonds, lead to the closing of many banks.

Page 34, line 23 following, and page 35: It occurs to us that if the provisions set forth in the bill should be adopted, it would be utterly impracticable to attempt to require compliance with the provisions of this section within the space of two years, as the results commanded could not be accomplished.

(11) Section 17 of the bill, page 38, lines 17 to 23: Here again we would call attention to the need of defining affiliates more narrowly than is the case in the definition of affiliates in section 2 of the bill or in this section with respect to the certificate of stock of national banks representing the stock of any other corporation. "Other corporation" seems too broad, as we have previously indicated several different types of corporations which might properly be affiliated with banks.

This restriction should not apply to those corporations whose principal purpose of existence is to relieve the bank of assets, acquired through the normal conduct of business and which assets it is not wise for the bank to retain.

(12) Section 18, page 39, line 12 following: The language contained in subdivision (c) is so sweeping as to warrant in our judgment the view that it may include banks within the category of those businesses toward which the prohibitions are directed. We feel that the provisions of this section go too far in the attempt to regulate business relationships of banks. We sympathize with the purpose of restricting funds available for stock exchange loans, but these provisions, if adopted, would restrict member banks, while leaving non-member banks and private individuals free to engage in the business of handling stock exchange loans defined as "loans for others."

(13) Sections 19 and 20 of the bill, page 39 following: We believe that sections 19 and 20 should be combined into one section. We have no objection to the requirements set forth in section 20, but instead of the sweeping prohibition now contained in section 19 there should be no restrictions upon the voting of shares of stock by an affiliate where the requirements now contained in section 20 are complied with.

We have no objection to the requirements expressed in section 20 being made a statutory condition upon the right of affiliates to vote, but we believe that, such statutory limitations being complied with, the Federal Reserve Board should not have any discretionary power to withhold or to revoke any permit.

(14) Section 24 of the bill, page 47, line 16 following. We do not believe that it is wise or necessary to regulate further by-law the rate of interest that may be paid upon deposits. From the standpoint of competition of member banks with nonmember banks, the former would be put at a decided disadvantage, with such regulations in force.

(15) Section 25, paragraph (c), page 49, lines 11 to 18. The requirement that each affiliate shall be capitalized through the sale of its own stock is too sweeping, for numerous affiliates have already been so capitalized. Such affiliates have not been capitalized through cash or stock dividend declarations on the part of the banks, but their stock has been subscribed and paid for, wholly or in part, by the individual stockholders. The proposed provisions of the bill would require, first, that the corporation should be liquidated and its capital assets returned to the stockholders, and second, that the stockholders should repurchase the stock of the reconstituted corporation.

We wish to reiterate our previous statements with respect to the need of restricting the definition of affiliates more narrowly than is the present definition in section 2.

(16) Section 26, page 49, line 22 following: This section is subject to the same objections made to section 8 of the bill.

Respectfully submitted.

EDWARD ELLIOTT, *Chairman.*
W. R. WILLIAMS, *Vice Chairman.*

X