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OPERATION OF THE NATIONAL AND FEDERAL RESERVE BANKING SYSTEMS

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Mr. NORBECK, from the Committee on Banking and Currency, submitted the following

MINORITY VIEWS

[To accompany S. 4412]

The Senate Committee on Banking and Currency has had under consideration the bill (S. 4412) 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, and reported favorably thereon on April 22, 1932. (Rept. No. 584.)

On behalf of the minority of the members of the Senate Committee on Banking and Currency, I am making this report in protest against the proposed extension of branch banking, without taking issue with the distinguished author of the bill, Senator Glass, on other matters in the bill, in most of which I heartily concur, and some of which I deem very important.

In speaking of our banking system, we must keep in mind that we have:

(1) A system of national banks chartered and supervised by the Federal Government.

(2) We have a competitive system, that of State banks, chartered and supervised by the States.

There is difference of opinion among well-informed people as to their comparative merits, and certainly there is a great desire on the part of certain people to wipe out the State banking system. What can not be done directly by law may be done by giving the national system such an advantage that the competitive State system can not exist.

Aside from the two general classifications, we might make further classifications, as follows: Unit bank, chain banks, group banks, branch banks.

A unit bank may have a national or State charter. It is generally defined as an institution which is owned, controlled, and operated by residents where the bank is located, and has no affiliated institutions. This is the typical American bank.

The term "chain bank" is generally applied where two or more banks are owned and controlled by one individual and partnership (without a holding company or more centralized control).

Group bank is the proper term for institutions that have been growing up in many sections of the country of late years. If not a violation of law, it is certainly an evasion of law. A holding company is generally organized for the purpose of owning and controlling these banks. As a rule, the holding company owns over 90 per cent of such bank stock, but there remains a local organization and a local board of directors, subject, however, to the control of the holding company, which is located in some central place.

It is a well-known fact that shares in a bank carry a double liability with them on the part of the stockholder. As a rule, the shares in a holding company do not carry this extra liability, though there are a few notable exceptions to this practice. I have in mind especially the Detroit group, who appeared before this committee and explained their system.

Branch banking is where a parent bank has one financial structure, from which it operates the several branches or offices under set rules and instructions issued by the head office. The officers of the several branches have very limited powers of discretion.

FALLING PRICES

Since the war, there has been a continual shrinkage in values and this has put a great strain upon our banking structure. Numerous failures have been taking place, and those, who for different reasons prefer the chain bank with the central control, are continually pointing to the banking systems of other countries. But all things considered, the American system has held up wonderfully well. Our Government has not come to the direct aid of our banking structure, such as has been the case in many European countries, where the governmental form of banking exists, where the taxpayers took the losses.

We are often reminded of the losses suffered by depositors in this country. That is true, and it is deplorable, but it is not fair to point to other countries for comparison. The American dollar is still at par, while the bank deposits in foreign lands have dwindled in proportion to the shrinkage of their currency value; in Canada it is 20 per cent, and in France it is 80 per cent. We have much over which to be happy, and do not need to be hasty about importing a banking system from foreign lands.

The so-called safety of the French, Canadian, or English system is simply one of percentage, and we need not be ashamed of the comparison.

It is not believed that the remedy lies in more centralization. When we take the history of the chain bank, group bank, and branch bank, many States in the Union have had debacles, which are appalling. The greatest bank failure in this whole depression was in the case of a branch-bank system—a central bank with some 50 or 60 branches. On the other hand, while the losses of unit banks in the

United States, due to overbanking conditions and the present financial situation, have been devastating, we have no assurance that such a condition may not arise again under a different form of banking, as each generation must learn its own lesson, and human nature, as a rule, has never been able to capitalize 100 per cent from the mistakes of the past.

BRANCH BANKS

Advocates of the branch-banking system ignore the fact that such a system has never been tried in a country of 120,000,000 population, 3,000 miles across. They ignore the tendency in this country to centralize control of everything, and especially of credit. I believe the branch-banking system would put us at the mercy of the financial centers.

THE CANADIAN SYSTEM

We hear much about the Canadian systen, which is the outgrowth of the British system, but we hear only the good side of it. However, we occasionally run across something suspicious even in these presentations. We are told that Canada has only 11 banks, with an average of about 400 branches, and that there have been no failures. This statement is not in accordance with the record, for they have had numerous failures.

An advocate of the Canadian system in a recent magazine article said they had had only 16 failures in 62 years. The branches are not counted when the failures occur, but let us take them at their own statement. They have 11 banks and they have had 16 failures; that is more than a hundred per cent.

We are told that these 11 Canadian bankers have during the last few years had a smaller percentage of failures than the banks in this country, and I think that is true. But we have a large number of banks in this country that have had no failures, and certainly we have one banking system here, not above referred to, that has gone through entirely without losses, and it has done an enormous banking business. The worst thing that can be said about it is that it has not furnished accommodation to the communities where the deposits were received. They have taken no risk. They have not been interested in building up the communities. If we had only such a system, we would make no progress in our development; we would slow down—we would come to a standstill. The system is the nearest comparable to the Canadian system. I have reference, of course, to the postal savings bank that drains the community dry of its cash.

One of our distinguished Senators, who has spent a great deal of time in Canada, told me privately he believed the natural resources of Canada were equal to those of the United States. Their growth has only been one-tenth the growth of the United States. I believe we are much indebted to the unit banking system for this difference.

I feel that section 19 of the Glass bill should be eliminated in its entirety. There is a movement on foot to control the banking industry of the United States by centralization. This movement might be termed not only national but international. Of late years this movement has been becoming more evident. The only way it can be accomplished, apparently, is through nation-wide branch banking and the complete elimination of the unit bank.

The unit banker has had a most prominent place in the development of the United States. By reason of his individualistic characteristics he has been able to mold himself to meet any possible situation. It has been through his foresight, strength of character, and belief in these great United States of ours that our country has become the foremost in commerce and industry. His endeavors have been most outstanding. The history of our country might have been different if our banking system had been controlled from Washington or New York.

Our dual system of banking has been one of the great motivating factors in making the United States the outstanding country that it is to-day. Our country is too large, too widely diversified, to expect one banking system to be so versatile as to deal with so complex a situation efficiently. The American people are individualistic and so should be our banking structure. The unit bank has a most definite position in our national welfare.

Two reasons have been advanced why we should have one system of banking:

First. The commerce of the United States should be financed in an orderly manner; must have a uniform system of banking under Federal supervision. Our past history does not prove the necessity of the same.

Second. That the Federal Government can not rely upon the voluntary cooperation of State banks and trust companies for the execution of a national policy. The record is clear that there has never been a time when the unit bank or the State chartered institutions have not upheld the hands of our Government.

The placing of our banking structure with the now overburdened bureaucracy in Washington is in direct violation of the principle of State rights. So far no tangible evidence has been offered that the passage of this section would be of value to the rank and file of our citizenry or would meet and stabilize the present situation. We have always the matter of politics, change of administration, Government in business, which can not be overlooked. History repeats itself.

The past several years a large amount of propaganda has been fed to the people endeavoring to educate them to national branch banking, and while the resolutions of some of our financial organizations were rapid in their opposition to branch banking, owing to steady pressure from without and within, their position has been gradually changing.

This plan appears to be a part of the preconceived plan for the elimination of the unit State bank and placing the control of our banking structure in financial centers. Those interested in controlling the banking structure of our country will find it far more easy to handle Washington than some 19,000 different banking corporations scattered throughout the United States. When banking and credit are centralized in a few hands, it is easier for the powerful to get control of such corporations; in fact, Mr. Whitney, president of the New York Stock Exchange, testified before the Banking Committee that with good dollars he could "go out and buy every corporation in the world," and there seems to be no limit to the number of good dollars they control. This is most true.

DEMANDS FOR MORE POWER

Congress first allowed the national banks to have branches within the city in which they were located. The next step was to allow branches in metropolitan areas. Now the demand is made that we have what will mean nation-wide branch banking in its entirety, and plans have been offered which can be utilized in eliminating every unit bank by direct congressional action.

It is in the interest of the United States that a banking monopoly should not be created. The theory of syphoning credits through a branch banking system has been exploded. Theoretically, it functions perfectly, until under pressure the pipe springs a leak. When a unit bank closes, there is merely a pop; when a system of branch banks closes, it is a detonation.

We only have to look back to the history of the endeavor to renew the charter of the Bank of the United States with its branches in the then leading cities, during the Presidency of Andrew Jackson, to prove now, as then, that a banking monopoly headed at Washington is not for the best interests of the citizens of the United States.

The placing of more power in the national banking system is dangerous. Additional powers given this system would not redound to its benefit, unless it is coupled with legislation that will cripple or eradicate our present State-chartered institutions. This fear of centralization in the hands of a few is possibly one of the factors behind the popularity of State-chartered institutions, and general satisfaction of our dual system of banking.

The following figures speak for themselves:

On December 31, 1931, there were in the United States 194 private banks, 587 mutual savings banks, 546 stock savings banks, 1,245 loan and trust companies, and 11,240 State banks; total, 13,812.

The national system had 6,368 banks with capital from $10,000 up, of which less than 225 had a capital of $1,000,000 or over.

As of the same time, national banks had on deposit $19,210,000,000, which included $260,000,000 of funds of the United States. While deposits of State-chartered institutions were $30,486,000,000, a difference of $11,175,000,000 in favor of State-chartered institutions.

Now as to capital structure: State-chartered institutions had $175,000,000 more than national banks and a surplus of $1,700,000,000 in excess of those of national charter. In other words, State-chartered institutions had more millions of surplus above the amount of surplus of national banks than the total aggregate of capital and national banks.

Further, take the period from March 25, 1931, to December 30, 1931. We find that during the intervening period, the deposits in national banks decreased $3,100,000,000, while deposits in State-chartered institutions decreased $3,700,000,000. The per cent of decrease in each instance is, national banks, 13 per cent; State banks, 8 per cent.

Now, further, a comparison of national bank suspensions and State bank suspensions:

In 1931, prior to the figures cited above, there were 409 bank suspensions as against 161 for the year 1930, or an increase of 154 per cent. While the State-chartered institutions had 1,809 suspensions in 1931, as opposed to 1,128 in 1930, or an increase of 60 per cent, there were reopened in 1931, 25 national banks and 250 State-chartered institutions, or 10 to 1. In 1930, there were reopened five national banks and 140 State-chartered institutions.

Now as to deposits: Time deposits in national banks, including deposits of the Post Office Department in national banks on December 30, 1931, were $7,594,000,000, as opposed to time deposits in State-chartered institutions of $18,430,000,000, or, roughly speaking, two and a half to one in State-chartered instututions. In the Postal Savings System, at the end of the last fiscal year, June 30, 1931, there was on deposit averaging $500 for each depositor, an aggregate of $347,000,000, an increase of $172,000,000 for the Government's fiscal year. Eight hundred and ten million dollars of the deposit shrinkage in State-chartered institutions were in savings accounts. The number of savings depositors decreased by one and a half million. Now, obviously, the million and one-half depositors who ceased having savings accounts in State-chartered institutions did not rush to the post office, for the increase in the number of postal-savings depositors during the same period was 304,000, or less than one-fifth.

LIQUIDATING CORPORATION

It is hoped that a liquidating corporation will be the means of more prompt payment to depositors of some substantial part of their equity as soon as a bank is closed. It is not a guaranty of bank deposits, though it may point in that direction and, therefore, be subject to much criticism.

GUARANTEE OF DEPOSITS

The State banking system is threatened from another angle, and that is the great demand now on the part of the national banks to have guarantee of deposits. The request is based on the plea that it will restore confidence, but I do not hesitate to say there are national banks that would like to unload their losses on the Federal Treasury, and among them are some large ones, and where the bank is a large one the taxpayer would be assuming a big burden. One of the purposes is to give the national bank a certain advantage over the State bank and destroy our dual system of banking. It is an indirect and an insidious way to do that which they dare not attempt to do directly.

The writer believes that guarantee of deposits may sometime become a reality, but it is quite convincing from the experience of many States that tried the bank guarantee law that a more careful approach to the subject must be made, and certainly it must be considered a form of insurance; therefore the two fundamental principles of insurance must be recognized:

(1) No loss must be underwritten which can not be paid.

(2) No risk should be assumed at 100 per cent value; 75 per cent would be a safer figure.

The depositor who could get 75 per cent cash would be fortunate, indeed, compared to some of those who wait many years on the slow liquidation of a receiver.

There are members of this committee who favor guaranty of bank deposits who would hesitate now to have the Government take over bank losses and also to destroy the State banking system, for State banks would not be included in the program for guaranty.

The depression, started in agricultural sections, brought down thousands of banks. These people have taken their losses. They protest against helping pay the losses that are now threatening other sections.

PETER NORBECK,
For the Minority.

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