

BUSINESS LOANS BY FEDERAL RESERVE BANKS

HEARINGS BEFORE A SUBCOMMITTEE OF THE COMMITTEE ON BANKING AND CURRENCY UNITED STATES SENATE

SEVENTY-SIXTH CONGRESS

THIRD SESSION

ON

S. 2998

A BILL TO ESTABLISH A PERMANENT INDUSTRIAL LOAN
CORPORATION TO ASSIST FINANCING INSTITUTIONS IN
MAKING CREDIT AVAILABLE TO COMMERCIAL
AND INDUSTRIAL ENTERPRISES

AND

S. 3839

A BILL TO AMEND SECTION 13b OF THE FEDERAL RESERVE
ACT, AS AMENDED

JUNE 12 AND 14, 1940

Printed for the use of the Committee on Banking and Currency



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CONTENTS

Statement of—	Page
Eccles, Marriner S., chairman, Board of Governors of the Federal Reserve System, Washington, D. C.-----	14
Jones, Jesse H., Administrator, Federal Loan Agency-----	44
Mead, Hon. James M., Senator from New York-----	7
Wiggins, A. L. M., president, Bank of Hartsville, Hartsville, S. C.; chairman, Committee on Federal Legislation of the American Bankers Association-----	31

EXHIBITS

Copy of S. 3839 and S. 2998-----	1
Letter addressed to Hon. John A. Danaher by Chairman Eccles, Federal Reserve Board-----	24
Letter addressed to Hon. Robert F. Wagner by D. W. Bell, Acting Secretary of the Treasury-----	26
Proposed amendment to section 13b of the Federal Reserve Act submitted by Mr. Bell-----	29
Letter addressed to Hon. Robert F. Wagner by Chairman Eccles, Federal Reserve Board-----	50

BUSINESS LOANS BY FEDERAL RESERVE BANKS

WEDNESDAY, JUNE 12, 1940

UNITED STATES SENATE,
SUBCOMMITTEE ON RECONSTRUCTION FINANCE
CORPORATION MATTERS OF THE COMMITTEE
ON BANKING AND CURRENCY,
Washington, D. C.

The subcommittee met at 10:30 a. m., pursuant to call, in room 301, Senate Office Building, Senator Robert F. Wagner presiding.

Present: Senators Wagner (chairman of the subcommittee), Adams, Clark of Idaho, Downey, Hughes, and Tobey.

Present also: Senators Danaher and Mead.

Senator WAGNER. The subcommittee will come to order. This meeting is for the purpose of a hearing on S. 3839, introduced by Senator Mead. And I take it, Senator Mead, that you wish a copy of the bill made a part of the record.

Senator MEAD. Yes; Mr. Chairman. I also may speak in regard to S. 2998, introduced by me last October.

Senator WAGNER. The bills will be made a part of the hearing. (The bills referred to, S. 3839 and S. 2998, are as follows:)

[S. 3839, 76th Cong. 3d Sess.]

A BILL To amend section 13b of the Federal Reserve Act, as amended

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 13b of the Federal Reserve Act, as amended, is amended to read as follows:

"Sec. 13b. (a) In exceptional circumstances, when it appears to the satisfaction of a Federal Reserve bank that a business enterprise located in its district is unable to obtain requisite financial assistance on a reasonable basis from the usual sources, the Federal Reserve bank, pursuant to authority granted by the Board of Governors of the Federal Reserve System, may make loans to, or purchase obligations of, such business, or may make commitments with respect thereto, on a reasonable and sound basis.

"(b) Each Federal Reserve bank shall also have power to discount for, or purchase from, any bank, trust company, mortgage company, credit corporation for industry, or other financing institution operating in its district, obligations of any business enterprise; to make loans or advances direct to any such financing institution on the security of such obligations; and to make commitments with regard to such discount or purchase of obligations or with respect to such loans or advances on the security thereof, including commitments made in advance of the actual undertaking of such obligations. Each such financing institution shall obligate itself to the satisfaction of the Federal Reserve bank for at least 10 per centum of any loss which may be sustained by such bank upon any of the obligations acquired from such financing institution, the existence and amount of any such loss to be determined in accordance with regulations of the Board of Governors of the Federal Reserve System: *Provided*, That in lieu of such obligation against loss any such financing institution may advance at least 10 per centum of such advance of credit without obligating itself to the Federal Reserve bank against loss on the amount advanced by the Federal Reserve bank: *Pro-*

vided, however, That such advances by the financing institution and the Federal Reserve bank shall be considered as one advance, and repayment shall be made pro rata under such regulations as the Board of Governors of the Federal Reserve System may prescribe.

"(c) The aggregate amount of loans, advances, and commitments of the Federal Reserve banks outstanding under this section at any one time, plus the amount of purchases and discounts under this section held at the same time, shall not exceed the amounts paid to the Federal Reserve banks by the Secretary of the Treasury under subsection (d) of this section, except that when the amounts so paid by the Secretary of the Treasury are, in the judgment of the Board of Governors of the Federal Reserve System, inadequate for operations under this section, the Federal Reserve banks, with the approval of the said Board, may continue operations under this section through the utilization of their other funds until the amount of such other funds so utilized equals the amounts received by them from the Secretary of the Treasury. All operations of the Federal Reserve banks under this section shall be subject to such regulations as the Board of Governors of the Federal Reserve System may prescribe.

"(d) In order to enable the Federal Reserve banks to make the loans, discounts, advances, purchases, and commitments provided for in this section, the Secretary of the Treasury is authorized and directed to pay to each Federal Reserve bank not to exceed such portion of the sum of \$139,299,557 as may be represented by the amount paid by each Federal Reserve bank for stock of the Federal Deposit Insurance Corporation, and not already paid to a Federal Reserve bank under the provisions of this section, upon request by the Board of Governors of the Federal Reserve System, in such amounts and at such times as the Board of Governors deems necessary to enable the Federal Reserve banks to make the loans, discounts, advances, commitments, and purchases authorized by this section, and upon execution by each Federal Reserve bank of an agreement (to be endorsed on the certificate of such stock) to hold such stock unencumbered and to pay to the United States all dividends, all payments on liquidation, and all other proceeds of such stock, for which dividends, payments, and proceeds the United States shall be secured by such stock itself, up to the total amount paid to each Federal Reserve bank by the Secretary of the Treasury under this section. Payments heretofore made by the Secretary of the Treasury to any Federal Reserve bank under the provisions of this section shall be subject only to the terms of the section as now amended. The Board of Governors of the Federal Reserve System shall have authority to reallocate among the Federal Reserve banks the funds received from the Secretary of the Treasury as said Board may find necessary in order to meet existing needs. Whenever the Board of Governors of the Federal Reserve System shall conclude, either as a result of a decrease in the volume of operations or otherwise, that the amounts paid to the Federal Reserve banks by the Secretary of the Treasury under this section are no longer needed for operations under this section, the total amount received from the Secretary of the Treasury under this section, after making adequate provision for losses incurred in the use of such amount and after adding any net income derived from the use of such amount, shall be paid to and become the property of the United States, such payments to be made as orderly liquidation of assets acquired through the use of such amount, as in the judgment of the said Board, will permit. All amounts required to be expended by the Secretary of the Treasury in order to carry out the provisions of this section shall be paid out of the miscellaneous receipts of the Treasury created by the increment resulting from the reduction of the weight of the gold dollar under the President's proclamation of January 31, 1934; and there is hereby appropriated, out of such receipts, such sum as shall be required for such purpose."

[S. 2998, 76th Cong., 2d sess.]

A BILL To establish a permanent industrial loan corporation to assist financing institutions in making credit available to commercial and industrial enterprises

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 13b of the Federal Reserve Act is amended to read as follows:

"Sec. 13b. (1) This section may be cited as the 'Industrial Loan Corporation Act'.

"(2) There is hereby created a body corporate with the name Industrial Loan Corporation (hereinafter called the Corporation). The principal office of the

Corporation shall be located in the District of Columbia, but it may designate and utilize as its agents for the performance of its functions any or all of the Federal Reserve banks, which are hereby authorized to act in such capacity, may establish branch offices, or may designate and utilize other persons or other existing institutions as its agents for the performance of its functions. The Corporation shall have power (a) to adopt, alter, and use a corporate seal, which shall be judicially noticed; (b) to have succession until dissolved by Act of Congress or in accordance with subsection (16) of this section; (c) to sue and be sued, complain and defend, in any court of law or equity; (d) to make contracts and to lease or acquire such real estate and equipment as may be necessary for the transaction of its business; (e) to prescribe by its board of directors bylaws and rules, regulations and requirements, not inconsistent with law, as to the manner in which its business and operations may be conducted and the powers granted to it by law may be exercised and enjoyed. The Corporation may exercise all powers specifically granted by this section and such incidental powers as may be reasonably necessary to effectuate the provisions of this section in accordance with its purposes and to prevent evasions of such provisions. All rules and regulations of the Corporation shall be prescribed by the board of directors and all determinations of matters of general policy for the Corporation shall be made by the board of directors; but it is the sense of Congress that in the administration of the Industrial Loan Corporation Act the Corporation shall endeavor to decentralize its activities, and all functions of the Corporation other than the prescribing of rules and regulations and the determination of matters of general policy may be performed through such members of the board of directors, such Federal Reserve banks, or such officers, employees, or representatives as the board of directors may prescribe; and the board of directors shall not be required to authorize, approve, or otherwise pass upon individual transactions.

"(3) For the purpose of providing funds to a commercial or industrial business, the Corporation is authorized, subject to such regulations and requirements as it may prescribe, (a) to make loans, to discount obligations for, and purchase obligations from such a business; (b) to purchase preferred stock in a corporation engaged in such a business; (c) to discount for or purchase from a financing institution obligations of, or preferred stock in a corporation engaged in, such a business; (d) to make loans to a financing institution on the security of such obligations or preferred stock; and (e) to make commitments to make any such loans, discounts, or purchases. The Corporation shall not make or acquire any such loan or obligation which has a maturity exceeding ten years, nor shall the Corporation purchase any such preferred stock unless the issuer of the preferred stock is obligated to retire the same within ten years; and all such loans, obligations, or preferred stock shall provide in a manner satisfactory to the Corporation for installment payments on the loan or obligation, or periodic retirements of the preferred stock, sufficient to amortize at least 40 per centum of the principal amount within a period of ten years. The Corporation may include in its regulations, among other things, provisions regarding the kinds of preferred stock which it may acquire, and regarding the purchase price of obligations and preferred stock and the rates of interest and discount applicable to transactions hereunder, and may define for the purposes of this or other subsections of this section the terms 'commercial or industrial business', 'financing institution', 'obligation', and 'preferred stock'. The Corporation may exercise the authority granted in this subsection either directly or in cooperation with financing institutions; but the amount of funds provided by the Corporation pursuant to this subsection for any one commercial or industrial business and outstanding at any one time shall not exceed \$1,000,000.

"(4) The Corporation is authorized and empowered to issue its notes, debentures, bonds, or other such obligations, which may be redeemable at the option of the Corporation before maturity in such manner as may be stipulated in such obligations, and shall mature at such times, be so secured, and bear such rate or rates or interest as may be determined by the Corporation. The aggregate of all obligations issued under this section and outstanding at any one time shall not exceed \$500,000,000. Such obligations may be issued in payment of any loan, discount, or purchase authorized by this section or may be offered for sale at such price or prices as the Corporation may determine. Such notes, debentures, bonds, or other such 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, such notes, debentures, bonds, or other such obligations, the Secretary of the Treasury shall pay to the holder the amount thereof which is hereby authorized to be appro-

printed, out of any moneys in the Treasury not otherwise appropriated, and thereupon to the extent of the amount 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. The Secretary of the Treasury, in his discretion, is authorized to purchase any notes, debentures, bonds, or other such obligations of the Corporation issued hereunder and for such purpose the Secretary of the Treasury is authorized to use as a public-debt transaction the proceeds from the sale of any securities hereafter issued under the Second Liberty Bond Act, as amended, and the purposes for which securities may be issued under such Act, as amended, are extended to include any purchases of the Corporation's notes, debentures, bonds, or other such obligations hereunder. The Secretary of the Treasury may, at any time, sell any of the notes, debentures, bonds, or other such obligations of the Corporation acquired by him under this section. All redemptions, purchases, and sales by the Secretary of the Treasury of the notes, debentures, bonds, or other such obligations of the Corporation shall be treated as public-debt transactions of the United States. The Corporation shall have power to purchase at any time and at any price any of the obligations issued by it, and any such obligations so purchased may be sold or resold at any time and at any price.

"(5) The Corporation is also authorized to borrow from any Federal Reserve bank, and any Federal Reserve bank is authorized to make advances to the Corporation, on the latter's promissory notes having maturities of not more than four months which are secured to the satisfaction of such Federal Reserve bank, at rates of discount established in accordance with the provisions of subsection (d) of section 14 of this Act and subject to such rules and regulations as the Board of Governors of the Federal Reserve System may prescribe.

"(6) The Corporation is authorized and empowered from time to time to set aside such amount, not exceeding \$25,000,000, of its surplus as it may deem advisable as an insurance fund, for the purpose of insuring banks whose deposits are insured under section 12B of the Federal Reserve Act, against losses which they may sustain upon obligations which they may acquire on or after the date on which the Industrial Loan Corporation Act becomes effective from any commercial or industrial business for the purpose of providing funds to such business. Such insurance may be granted to any such bank in such circumstances and upon such terms and conditions as the Corporation may by regulation or otherwise prescribe, including among other things limitations, to the extent deemed necessary, on the rate of interest borne by an insured obligation, on the amount of obligations insured for any one bank, on the types of obligations insured, and on the percentage of the total amount of the obligations of any type acquired by any one bank to which the insurance shall apply, and requirements for the payment of premiums by the insured banks; but no such insurance shall be granted to any one bank with respect to outstanding obligations of one obligor which exceed \$25,000, in amount, and each such insured obligation shall provide by its terms and on a basis satisfactory to the Corporation for amortization by payments which will extinguish the debt secured thereby within a period of not exceeding ten years.

"(7) The net earnings of the Corporation, after making adequate provision for losses, shall be transferred to its surplus or undivided profits account. Upon the liquidation or dissolution of the Corporation all assets remaining after the payment of all indebtedness of the Corporation shall be paid to and become the property of the United States.

"(8) The Corporation is authorized to sell, exchange, or otherwise dispose of any obligations or preferred stock which it has acquired, with or without its endorsement or guaranty and upon such terms and conditions as it may deem advisable. The provisions of the Securities Act of 1933 shall not apply to any obligations issued by the Corporation under subsection (4) of this section, nor to transactions by any person in connection with any acquisition by the Corporation of obligations or preferred stock or any commitment to acquire them under subsection (3) of this section, nor, after any such obligations or stock are so acquired by the Corporation, to any subsequent sale, exchange, or other disposition of them by any person.

"(9) Any and all notes, debentures, bonds, or other such obligations issued by the Corporation shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift 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, its franchise, loans and other assets, its capital stock, its surplus, its reserves, 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 other taxing authority; except that any real

property of the Corporation shall be subject to State, Territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed.

"(10) Notwithstanding any other provision of law, all suits of a civil nature at common law or in equity to which the Corporation shall be a party shall be deemed to arise under the laws of the United States, and the district courts of the United States shall have original jurisdiction of all such suits; and when the Corporation is a defendant in any such suit, it may, at any time before the trial thereof, remove such suit from a State court into the district court of the United States for the proper district by following the procedure for the removal of causes otherwise provided by law. No attachment or execution shall be issued against the Corporation or its property before final judgment in any suit, action, or proceeding in any State, county, municipal, or United States court.

"(11) The Corporation is authorized and empowered to take such steps as it may deem appropriate to encourage and assist in the formation of committees of representatives of small businesses and others in local communities to explain to possible or prospective applicants for funds the facilities of the Corporation provided in this section and to advise with and assist prospective applicants in connection with their requests for financial assistance from the Corporation.

"(12) The management of the Corporation shall be vested in a board of directors consisting of the members of the Board of Governors of the Federal Reserve System, and the chairman and vice chairman of the board of directors shall be the chairman and vice chairman, respectively, of the said Board of Governors. At meetings of the board of directors three members shall be necessary for a quorum. The Corporation may utilize, as its officers and employees, any employees of the Board of Governors of the Federal Reserve System, and any officers or employees of any Federal Reserve bank. If the Corporation shall find it advisable, it may employ additional officers or employees, and the employment, compensation, leave, and expenses of such additional officers and employees shall be governed solely by the provisions of this section, specific amendments thereof, and rules and regulations of the Corporation not inconsistent therewith. No director of the Corporation and no officer or employee of the Board of Governors or of any Federal Reserve bank shall receive any compensation from the Corporation by reason of any services which he may perform for it. The Corporation shall determine and prescribe the manner in which its obligations shall be incurred and its disbursements and expenses allowed and paid, and may deposit in any Federal Reserve bank its funds, which shall not be construed to be Government funds or appropriated moneys. The Corporation may invest its funds in direct obligations of, or obligations guaranteed as to principal and interest by, the United States. The Corporation shall reimburse the Board of Governors of the Federal Reserve System and the Federal Reserve banks and its other agents for their expenses in carrying out the provisions of this section on such basis as may be determined by the Board of Governors of the Federal Reserve System.

"(13) The Corporation shall have a capital stock and surplus which shall be paid in in the amounts and out of the funds hereinafter provided. The Secretary of the Treasury is hereby authorized and directed, on the date on which the Industrial Loan Corporation Act becomes effective, to purchase from each Federal Reserve bank the stock of the Federal Deposit Insurance Corporation heretofore subscribed for by such bank and to pay to such bank therefor an amount equal to the entire sum which the said Secretary was originally given authority to pay to such bank under the provisions of this section less the difference between the aggregate amounts paid to such bank by the Secretary of the Treasury and the aggregate amounts paid to the Secretary of the Treasury by such bank under the provisions of this section prior to the date on which the Industrial Loan Corporation Act becomes effective. When the payment of such amount has been made by the Secretary of the Treasury to such bank, the United States shall become and be the owner of all the stock in the Federal Deposit Insurance Corporation heretofore subscribed for or held by the said Federal Reserve bank and all rights of the said Federal Reserve bank with respect to said stock shall be transferred to and vested in the United States. Any and all of the obligations and liabilities to the United States and to the Secretary of the Treasury which have been imposed upon or incurred by any Federal Reserve bank under this section at any time prior to the date on which the Industrial Loan Corporation Act becomes effective shall on said date be completely discharged and terminated, and no Federal Reserve bank shall, after said date, have any obligation or liability to the United States or the Secretary of the Treasury by reason of any provisions of this section. The amount required to be paid to each Federal Reserve bank by the Secretary

of the Treasury under the provisions of this section shall be paid out of the miscellaneous receipts of the Treasury created by the increment resulting from the reduction of the weight of the gold dollar under the President's proclamation of January 31, 1934, and there is hereby authorized to be appropriated, out of such receipts, such sums as shall be required for this purpose.

"(14) Upon the receipt by each Federal Reserve bank from the Secretary of the Treasury of the amount specified in subsection (13) hereof, such Federal Reserve bank shall forthwith pay the entire amount so received to the Industrial Loan Corporation and also shall forthwith pay to the Corporation an amount equal to the difference between the aggregate amounts paid to such bank by the Secretary of the Treasury and the aggregate amounts paid to the Secretary of the Treasury by such bank under the provisions of this section prior to the date on which the Industrial Loan Corporation Act becomes effective; and out of the aggregate amounts paid to the Industrial Loan Corporation in this manner the Corporation shall set aside \$100,000,000 as its capital and the remainder as surplus and shall issue to and in the name of the United States, and deliver into the custody of the Secretary of the Treasury, capital stock in the amount of \$100,000,000. No stock in the Industrial Loan Corporation shall be transferable, have any voting rights, or be entitled to any dividends. Upon the payment of such funds to the Industrial Loan Corporation by the Federal Reserve banks, the Corporation shall forthwith purchase from each Reserve bank, and each Federal Reserve bank shall sell to the Corporation, all assets held by the Reserve bank which were acquired under the provisions of this section prior to the date on which the Industrial Loan Corporation Act becomes effective, and such sale shall, be made at the appraised value of the assets on the effective date of the Industrial Loan Corporation Act, such appraisal being made according to such rules and regulations as the Board of Governors of the Federal Reserve System may prescribe. All commitments of each Federal Reserve bank outstanding under this section on the date on which the Industrial Loan Corporation Act becomes effective shall forthwith be taken over and assumed by the Corporation.

"(15) When designated for that purpose by the Secretary of the Treasury, the Corporation shall be a depository of public moneys under such regulations as may be prescribed by said Secretary; and it may also be employed as a fiscal agent of the Government; and it shall perform all such reasonable duties, as depository of public money and fiscal agent of the Government, as may be required of it. Obligations of the Corporation shall be lawful investments, and may be accepted as security for all fiduciary, trust, and public funds the investment or deposit of which shall be under the authority or control of the United States or any officer or officers thereof. 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.

"(16) Whenever it shall appear to the Board of Governors of the Federal Reserve System, either by reason of a decrease in the volume of the operations of the Corporation or otherwise, that there is no longer a reasonable need for the continuance of the facilities of the Corporation, the said Board may order the dissolution of the Corporation, and thereupon the Corporation shall be liquidated and its affairs wound up under regulations prescribed by the said Board.

"(17) The Corporation shall annually prepare a full report of its operations, and this report shall be included by the Board of Governors of the Federal Reserve System in the annual report made by it to the Speaker of the House of Representatives in accordance with the provisions of section 10 of this Act."

Sec. 2. Subsections (h), (i), and (k) of section 22 of the Federal Reserve Act are amended by inserting after the words "Federal Reserve bank" wherever they occur in such subsections the words "or the Industrial Loan Corporation"; and subsection (j) of said section 22 is amended by inserting after the words "Federal Reserve bank" the words "and of the Industrial Loan Corporation".

Sec. 3. (1) The third paragraph of section 24 of the Federal Reserve Act is amended by striking out the word "established" where it appears in said paragraph, by substituting the words "the Industrial Loan Corporation" for the words "a Federal Reserve bank" wherever they appear in said paragraph, and by striking out the words "or (d) in which" which appear in said paragraph and substituting therefor the following: "(d) which are insured by the Industrial Loan Corporation, or (e) in which".

(2) The last sentence of paragraph "Seventh" of section 5136 of the Revised Statutes, as amended, is further amended by inserting before the colon after the words "national mortgage associations" a comma and the following: "or obligations of the Industrial Loan Corporation".

SEC. 4. Sections 1, 2, and 3 of this Act shall become effective on the 1st day of the second calendar month following the date of its enactment.

Senator WAGNER (chairman of the subcommittee). Senator Mead, we will be delighted to hear from you.

STATEMENT OF HON. JAMES M. MEAD, A SENATOR FROM NEW YORK

Senator MEAD. Mr. Chairman and members of the subcommittee, first of all I wish to tell you how deeply I appreciate this opportunity to appear here and speak in regard to this matter.

Your consideration of the bills which I have introduced has encouraged me to continue my effort to establish the opportunity for small-business men to enjoy the credit facilities that their bigger competitors have been enjoying right along.

We are all agreed that the industrial resources of the Nation must be coordinated and geared into a great productive machine which can produce quickly and efficiently the necessary weapons of national defense. We read over and over again that the time has arrived when opposing groups of our people must lay down their differences and strive for unity.

We do not know what productive necessities lie ahead, but it is not outside the realm of thoughtful consideration that the industrial agencies of this Nation may be called upon, as never before, to cooperate in supplying vital military equipment.

We hope with all our hearts that the economic resources of this Nation shall not have to be dissipated in the wasteful pursuit of rearmament. Nevertheless, this is no time for miscalculation nor for indifference to the gravity of world conditions.

With these unpleasant but realistic portents in mind, the Congress must assume earnest responsibility in providing for the well-being of certain branches of our industrial system which have been surviving with great difficulty during the past few years.

Senator ADAMS. Senator Mead, would an interruption bother you?

Senator MEAD. No.

Senator ADAMS. Do you mean to lay the foundation for your present effort upon the need for national defense, so that if the emergency should pass you would no longer have an interest in it?

Senator MEAD. No, that is not what I have in mind, but imperative is the great need for a national defense program. Having in mind the great part that the small-business man played in this same program in the World War, and realizing his desire to improve plant facilities so that he may take advantage of the opportunity to serve the Government in this crisis, prompted me to preface my remarks with that statement.

I realize that if the principle is established, if the system whereby small-business men may secure adequate credit facilities is established, then their plants, which will serve the Government in this crisis, will be in fine shape to continue peacetime operations, after the crisis is over.

Small business enterprise has been experiencing great difficulty in securing adequate long-term credit and capital at reasonable rates of interest. I am going to go into that subject further a little later in my remarks, but I predicate what I say now on the thought that little business is in extremely severe circumstances.

Now, it occurs to me that this is not a time when we, as a Nation, can afford to sacrifice any essential industries, large or small, that may contribute to our productive ability directly or indirectly in the provision of national defense requirements. In considering our great industrial power, the little business in a little plant in a little obscure community is just as vital and just as important as the great huge corporation with its far-flung branches. Little business is scattered in small villages and hamlets throughout the Nation, but, even so, little business is, collectively, an empire all of its own. It is a strong arm on which the Nation must depend for strength in any national emergency.

It is an unfortunate circumstance that little business today, through a strangulation of credit and capital is, to a large extent, operating with antiquated machinery, with old processes, and has been reduced to a relatively low level of productive efficiency. The small business man supplies the raw materials which big business needs. Through his hands flow countless important articles with which we shall be more and more in need.

Therefore, what I say to you today about little business is of vast importance in this program of national defense upon which we are about to embark. We must strengthen the utility of little business, increase its productive efficiency, and revitalize its place in the economic sphere. If more adequate credit and capital through local banks is all that little business requires, and that is my conviction, we ought to immediately concern ourselves with the satisfactory disposition of this problem.

I want to read for you a very brief summary of the chief features of S. 2998—

Senator ADAMS (interposing). We only have before us on the committee table S. 3839.

Senator MEAD. We also have S. 2998. I can take up S. 3839 first if you wish. These proposed amendments to section 13b of the Federal Reserve Act would eliminate certain limiting provisions. It is important that we have that in mind. Section 13b of the Federal Reserve Act now authorizes Federal Reserve banks to make loans direct to established commercial and industrial enterprises for working capital purposes for periods up to 5 years.

Senator ADAMS. Senator Mead, you speak of that as a limitation, and yet that is an expansion and departure from the original Federal Reserve Act.

Senator MEAD. It was, yes. When it was introduced and passed under the sponsorship of Senator Glass, it was a liberalization, at that time, but it is a severe limitation to restrict small business in the matter of loans for working capital purposes only for a period of 5 years when their bigger competitor can secure loans for unlimited periods and for all other purposes, I mean other than for working capital purposes.

I will take up this explanation of the proposed amendments to section 13b of the Federal Reserve Act as contained in S. 3839:

Section 13b of the Federal Reserve Act now authorizes Federal Reserve banks to make loans direct to established commercial and industrial enterprises for working capital purposes for periods up to 5 years. It also authorizes the Federal Reserve banks to grant commitments to or participate with financing institutions with respect

to any such loans. The limitations now contained in the act with respect to working capital, established businesses, and maturities make it impossible for the Federal Reserve banks to grant credit to many worthy enterprises, particularly where additional funds are needed for expansion or improvement.

The proposed amendment would eliminate these limiting provisions and permit Federal Reserve banks to extend credit to any business enterprise, without restriction as to purpose, for such periods as the circumstances in each case would warrant.

And I might say that that is the gist of the amendment. It is a liberalizing amendment.

Under present law the Secretary of the Treasury is authorized to pay to the Federal Reserve banks up to \$139,299,557, out of the increment resulting from the reduction of the weight of the gold dollar, for the purpose of enabling the Federal Reserve banks to make industrial advances. This is the amount paid by the Federal Reserve banks for stock in the Federal Deposit Insurance Corporation. The Secretary of the Treasury has paid to the Federal Reserve banks approximately \$27,000,000 for this purpose. The law now requires the Federal Reserve banks to pay the Government annually 2 percent, if earned, on the amount received from the Secretary of the Treasury. The proposed amendment would direct the Secretary of the Treasury to pay to the Federal Reserve banks when requested by the Board of Governors of the Federal Reserve System such portions of the sum of \$139,299,557, not already paid to the Federal Reserve banks, as the Board of Governors may deem necessary to enable the Federal Reserve banks to make the loans, discounts, advances, purchases, and commitments therein authorized, would eliminate the provisions for the annual payment by the Reserve banks of 2 percent, and would authorize the Board of Governors to make such reallocation among the Federal Reserve banks of funds received from the Secretary of the Treasury as it may find necessary to meet existing needs.

The amendment also provides that whenever the Board of Governors of the Federal Reserve System shall conclude that the amounts paid to the Federal Reserve banks by the Secretary of the Treasury are no longer needed for operations under section 13b, the amount received from the Secretary of the Treasury, plus income and less expenses and losses, shall be paid to and become the property of the United States.

The amendment eliminates the requirement of the present law that each Federal Reserve bank shall have an industrial advisory committee to pass on all loan applications.

Senator ADAMS. What is the objection to that?

Senator MEAD. It was suggested in the interest of better administration and to facilitate the issuance of loans. It is hoped that Federal Reserve banks, and the Federal Reserve Board, through its regulations and instructions, would cut red tape and permit the functioning of this liberalizing amendment to the end of expediting the issuance of loans. In other words, it would expedite the volume of loans required for small businesses.

Under the present section 13b each financing institution obtaining a commitment from or participating with a Federal Reserve bank on any loan must bear at least 20 percent of any loss that may be sus-

tained. The proposed amendment would modify this to provide that the financing institution must bear at least 10 percent of any loss that may be sustained on such a loan.

Now, Mr. Chairman and members of the subcommittee, that is an explanation of the bill, S. 3839. I might say that it is the more modest approach to the problem I have in mind.

As I mentioned awhile ago, there is another bill here, S. 2998, which is also suggested as an approach to the solution of this problem. It embodies not only the philosophy of the bill I have just explained but it sets up an industrial loan corporation within the Federal Reserve System, or by that System, to make loans to business through this proposed corporation. It establishes a system of coordinating business loans, and it would permit the corporation to borrow, sets forth regulations for the management of the corporation, and for the dissolution of the corporation when it is no longer needed. It requires an annual report to be made to the Congress of its activities, to be submitted by the Federal Reserve Board.

Senator WAGNER. Do you want us to consider both of these bills?

Senator MEAD. Well, this is a minor modification of the existing section. In view of the lateness of the session it is quite possible that such a proposal could get further than the major proposal.

Senator WAGNER. When you say "such a proposal" you mean S. 3839.

Senator MEAD. Yes. That is the minor proposition. And the bill S. 2998 is the major proposal. I have here an explanation of that bill, which is only two pages long, if I may read it?

Senator WAGNER (chairman of the subcommittee). We will be glad to hear it.

Senator MEAD. This is an explanation of S. 2998, which is referred to as the Industrial Loan Corporation bill.

Industrial Loan Corporation: The bill would terminate the present limited authority of the Federal Reserve banks to make industrial loans, and would transfer this authority, in broadened and more effective form, to the Industrial Loan Corporation, which the bill would set up as an integral part of the Federal Reserve System. The activities of the Corporation could be promptly set in motion through the existing facilities of the Federal Reserve System. The plan would involve no increase in the Budget.

Loans to business by Corporation: The Corporation could extend financial assistance to commercial or industrial businesses by acquiring their notes, debentures, bonds, or similar obligations, by purchasing preferred stock in such businesses, or by making commitments to acquire such obligations or stock. Such obligations could not have a maturity in excess of 10 years and provision would have to be made, in a manner satisfactory to the Corporation, for periodic repayments or retirements on such obligations and stock sufficient to repay or retire at least 40 percent of the principal amount within a 10-year period. The Corporation could extend its assistance to industrial or commercial businesses directly or in cooperation with financing institutions, but it could not have more than \$1,000,000 of funds outstanding at any time to any one commercial or industrial business.

Senator ADAMS. This would go beyond the lending field and provide for investments. That is, it would provide that the proposed institutions may purchase preferred stock, which is an entire departure from the credit-extending feature.

Senator MEAD. Well, of course, it is assumed that it will have power similar to the power of the Reconstruction Finance Corporation, and that it will be able to make such purchases in the interest of the safety of the investments of the United States. These investments will permit the business enterprise to expand and to rehabilitate present plants; at the same time it will probably prove safer than an outright loan.

Senator ADAMS. Is there not a very wide distinction between the situation of the R. F. C. and Federal reserve banks? The capital of such banks is contributed by private institutions. There you are dealing with capital furnished by private institutions. In the case of the R. F. C. the Government furnishes the credit. If the Government wants to do what it pleases with its own funds, that is one thing, but it is hardly a parallel to have banks buying preferred stock with money that belongs to the banks, and, in turn, you must remember the banks are dealing with money which belongs to their depositors.

Senator MEAD. I do not believe that we should delimit the operations of private banks, and if the Government is permitted to invade this field it seems to me the banks should be permitted also to invade this other field if it presents a lucrative opportunity.

Senator ADAMS. But this in substance would be compelling banks to take money of their depositors and invest it in preferred stock of industry.

Senator MEAD. We have another provision in the bill that permits of raising this money which will be at the disposal of the corporation. And in view of the fact that our banks are burdened with idle cash it seems to me we ought to be exploring every possible field for profitable investment.

Senator ADAMS. But we do not want to go into a field which will prevent banks from paying depositors their money. We do not want them placed in the position where they might have to say: We have some preferred stock, and how would you like to have that stock?

Senator MEAD. I believe the Federal Reserve Board, and the proposed corporation, which would be an integral part of the system, will be able to make liquid a sufficient amount of money to cover the requirements of depositors.

Senator DANAHER. Let me ask Senator Adams if his objection in that particular—

Senator ADAMS (interposing). It is a comment, not an objection.

Senator DANAHER. I understand that it was more in the nature of a comment. But let me consider it for my present purpose as an objection.

Senator ADAMS. All right, if you wish to do so for the purpose of your question.

Senator DANAHER. Would that objection be met if it were put on an optional rather than a compulsory basis, I mean with reference to the individual?

Senator ADAMS. There will be the option, I take it.

Senator DANAHER. Yes.

Senator ADAMS. But who will have the option?

Senator DANAHER. The Federal Reserve banks. I mean a Federal Reserve bank will have the option as to whether or not it will participate in the machinery they set up.

Senator ADAMS. That would take away a good deal of the objection. Here the Federal Reserve Board is appointed at Washington, and as

to the banks they elect the majority of the representatives, but the Board is the representative of the Federal Government.

Senator DANAHER. While I am not on this subcommittee yet I have attended almost every hearing that has been held on this subject, and am perfectly convinced there is a need for equity or investment capital somewhere. How we will provide it is the problem. Whether or not this bill does it is questionable. I agree with Senator Adams in his approach to this subject, now construing the present position as an objection, but I do think some means might be found whereby we might open an outlet for capital up to 5 years, or perhaps 10 years. Certainly today that is lacking in any number of fields, particularly with reference to small businesses.

Senator MEAD. In view of the condition of banks today—and we have read recently of banks forced to close their doors because of the drain upon their resources resulting from idle money—I think something must be done. In view of the safeguarding provisions included in this bill I think it would help the situation.

Senator ADAMS. I take it you would rather have a bank closed because of having too much money than because of not having enough money.

Senator MEAD. I think having banks that are overstuffed with money, and banks that have not enough money, are twin evils. Those are evils that have developed in the working out of our Democratic processes, and we have to find some outlet or our Democratic processes will probably be weakened. At any rate I can see no objection to the proposed corporation under the safeguarding influence of the Federal Reserve System enjoying the same privilege which the R. F. C. now enjoys as long as the investment is safe, as long as the liquid requirements of the system will be met.

Senator CLARK of Idaho. Referring to the lay-out provided for here in S. 2998, is that the set-up that was presented to the monopoly committee, the T. N. E. C., by Mr. Berle, I think it was?

Senator MEAD. I doubt it. It may have some relationship to it but it is not identical. Perhaps I better read further along here and thereby I may answer some of your questions.

Insuring business loans: The corporation could set aside an amount not exceeding \$25,000,000 as an insurance fund for insuring banks whose deposits are insured by the Federal Deposit Insurance Corporation against losses which such banks may sustain on future loans to commercial or industrial businesses. The corporation could prescribe regulations regarding such matters as limitations on the rate of interest on insured loans, the types of obligations insured, the percentage of total obligations of any bank which would be insured, and premiums to be paid for the insurance, but no such loan could be insured unless it was for an amount not exceeding \$25,000 and was to be amortized over a period not exceeding 10 years.

Capital and surplus of corporation: The capital and surplus of the Industrial Loan Corporation would be supplied from a fund of about \$139,000,000 which has already been appropriated (out of the increment resulting from the devaluation of the dollar) for the purpose of assisting Federal reserve banks in making industrial loans. The Secretary of the Treasury was authorized to pay this sum to the reserve banks for this purpose on the security of the approximately \$139,000,000 of Federal Deposit Insurance Corporation stock which

the reserve banks were required to purchase when the Federal Deposit Insurance Corporation was organized.

Senator ADAMS. With that provision these two bills do not go along parallel. That is, this major bill would exclude the other because otherwise you would be making use of the same fund twice.

Senator MEAD. Oh, yes; you could not have the two bills. What I am concerned with is securing a bill at this session, and if this bill is too complicated I prefer the minor and less complicated bill.

Senator WAGNER. I was just looking at this bill, S. 3839. That does not provide for any purchase of preferred stock.

Senator MEAD. Oh, no; I will continue with this explanation of S. 2998:

Pursuant to this authority, the Secretary has paid approximately \$27,000,000 to the reserve banks and the proposed plan would require him to pay the balance, or about \$112,000,000. The reserve banks would be required to use all of these funds to supply the capital and surplus of the Industrial Loan Corporation which would consist of about \$39,000,000 of surplus and \$100,000,000 of capital stock, to be issued to the United States and delivered to the Secretary of the Treasury. The Federal Deposit Insurance Corporation stock now owned by the Federal reserve banks would also be transferred to and be owned by the United States. The outstanding industrial loans and commitments of the Federal reserve banks would be transferred to the Industrial Loan Corporation. Upon the dissolution or liquidation of the Industrial Loan Corporation all its assets in excess of indebtedness would be paid to the United States.

Borrowing by Corporation: The Corporation could issue notes, debentures, bonds, or similar obligations to the amount of \$500,000,000, and such obligations would be guaranteed as to principal and interest by the United States and would have tax exemptions similar to those of other Government guaranteed obligations. The Corporation also could borrow from any Reserve bank on the Corporation's promissory note secured to the satisfaction of the Reserve bank and having a maturity not exceeding 4 months.

Management of Corporation: The members of the Board of Governors of the Federal Reserve System would be the directors of the Industrial Loan Corporation and the chairman and vice chairman of the Board of Governors would be chairman and vice chairman, respectively, of the Corporation. The Corporation could utilize the Federal Reserve banks as its agents, and could use any employees of the Board of Governors or the Reserve banks as its own officers or employees, reimbursing the Board of Governors or the Reserve banks for such services. No director of the Corporation and no officer or employee of the Board of Governors or of any Reserve bank would receive any extra Compensation for his services for the corporation. The bill provides that the Corporation "shall endeavor to decentralize its activities" and that functions other than the prescribing of regulations or the determination of general policies may be performed through designated representatives.

Dissolution of Corporation when not needed: The Board of Governors of the Federal Reserve System could order the dissolution and liquidation of the Corporation whenever it appears, either by reason of decreased volume or otherwise, that there is no longer a reasonable need for the facilities of the Corporation.

Small-business men's committees: The Corporation would be authorized to take appropriate steps to encourage and assist in the formation of committees of representatives of small business and others in local communities to explain the corporation's facilities and assist prospective borrowers in presenting their applications.

Annual report: A full report of its operations would be made by the Corporation annually and included in the annual report submitted to Congress by the Board of Governors of the Federal Reserve System.

Now, Mr. Chairman, I understand that your committee has a favorable report from the Federal Reserve Board on the similar bill, S. 3839. We also have present the chairman of the Federal Reserve Board and one of the members of the Board of Governors. If it is your desire—and it would meet with my approval I assure you—to take up S. 3839, we will dismiss S. 2998 with the explanation, which can be made a part of your record, and revert to the smaller bill, which has the approval of the Federal Reserve Board, namely, S. 3839, for our further discussion this morning.

Senator WAGNER (chairman of the subcommittee). Very well.

Senator MEAD. S. 3839 is the minor bill. It is the one that I developed in the first part of my talk, and that is the one that has the approval of the Federal Reserve Board.

Senator WAGNER. That is the bill which you desire the subcommittee to consider at this time.

Senator MEAD. It is my belief that that bill may get some place at this time, that it can make progress, that it does not require the study nor the effort on the part of the committee or of the Congress that the other bill might require. Therefore I think it would be the wisest choice for us to make; and because the chairman of the Federal Reserve Board is here I would like you to ask him to answer any questions or make any statement that he may desire to make.

Senator WAGNER. Very well. Have you concluded your statement, Senator Mead?

Senator MEAD. I have concluded, unless you have some questions?

Senator WAGNER. Any questions by members of the subcommittee? (A pause without response.)

We thank you very much, Senator Mead.

Now, Chairman Eccles, will you come forward to the committee table and give us the benefit of your views on S. 3839?

Mr. ECCLES I will be glad to do so.

Senator WAGNER. I think, before we ask you any questions, we would like you to give us your views generally on this proposed legislation.

STATEMENT OF MARRINER S. ECCLES, CHAIRMAN, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, WASHINGTON, D. C.

Mr. ECCLES. The Board has felt that the existing authority given to the Federal Reserve System to make direct loans to industry is entirely inadequate, and for that reason that, unless the law is amended, they should be entirely relieved of any responsibility in connection with making such loans by repealing the present provision of the law and authorizing them to liquidate the loans which they now

hold and the commitments which are outstanding to banks, thus returning to the Treasury the funds that have been advanced and upon which the Federal Reserve System is required to pay, if they earn it, 2 percent.

But in the absence of such a repeal, we feel that the Congress should give us broader powers to deal with this problem of making direct loans. It hardly seems fair to be charged with the responsibility and be unable to carry it out because of the great restrictions and limitations on loans.

We are not asking during my time, nor has the Federal Reserve System asked, for increased powers to enter this field. It is up to the Congress to determine whether or not they desire the Federal Reserve System to enter this field.

There has been considerable argument as to whether or not the Federal Reserve System should do this type of lending; whether the Reconstruction Finance Corporation should not do the lending in its entirety.

It seems to me there is this to be said in this connection: The direct lending was initiated in the first instance by Governor Black, who was the head of the Federal Reserve Board, in 1934, and it was as a result of his effort that this legislation was originally enacted.

The Reconstruction Finance Corporation, very shortly after the effort was made by Governor Black to get this power, also undertook to get a duplication of the authority to make this type of loan. So that from the beginning there has been a divided responsibility, or authority, to make loans of this sort.

There has been this exception, however: That the law governing the Reserve System's authority to make direct loans has not been amended since 1934 to meet the situation; whereas during that period there have been three or four important amendments to the R. F. C. law, and as a result, of course, the Reserve System has, for all practical purposes, for the past 2 or 3 years, I would say, been almost out of business in this particular field.

The Federal Reserve System, it seems to me, is particularly well organized and adapted to do a job of this sort. With 12 banks and 24 branches, making 36 offices, located in the trade areas throughout the United States, with the close relationship of those banks and branches to the member banks, and the member banks include all national banks and a large number of State banks, practically all of the larger State banks, we should be adapted to do this job. In other words, member banks of the Federal Reserve System that do business with these Reserve banks and branches constitute more than 85 percent; that is, they hold more than 85 percent, of the deposits of the banking system. These Reserve banks have been established for a period of 25 years. They have a trained staff of people who are well qualified and who, at the present time, have little to do in the field of credit, because the member banks, due to the larger excess reserves that they have had since the twenties, have little need for borrowing from the Reserve System; and this staff is what we may term a stand-by organization, and they could very well perform this function without any extra cost or expense. They have the facilities in the way of buildings, equipment, and so forth, and they have a very close daily relationship with the banks of the area and know the credit needs of the people better than anyone else of the area.

For that reason, it would seem to me that, under the direction of the Board for the purpose of carrying out a uniformity of policy and regulations governing loans, the Federal Reserve System is in a particularly good position to perform this function.

Now, the R. F. C. in a good many instances occupies quarters in the Reserve banks. They had to set up an organization to do this work. They have, of course, other fields of activities besides this, such as the taking of the preferred stock and debentures of banks, such as the specialized field of loans to railroads, and such as the specialized field that is recently proposed in the legislation to help finance the armament program. Those are large, specialized fields that I do not believe the Reserve System should go into, and they are not in any way, of course, contemplated under this proposed bill or under the other proposed bill that Senator Mead has discussed.

This bill, or the other bill, for that matter, contemplates pretty largely the loans being made by the local banks, the member banks in the area, with the commitment made by the Reserve System.

Senator DANAHER. May I interrupt you, Mr. Eccles?

Mr. ECCLES. Yes.

Senator DANAHER. Would you right at that point be willing to explain to us the commitment in loans now outstanding under the present section 13b and compare that particular situation with what could be done under section 13b as amended?

Mr. ECCLES. Yes; I will be glad to do that.

As Senator Mead has explained to you, the present law has very great limitations. First, the loans must be for working capital purposes and they must not exceed 5 years and they must be made on a reasonable and sound basis to established businesses. In other words, the law pretty generally confines the Reserve System to the type of lending that the banks themselves would make without the Reserve System.

There is the further feature that the Federal Reserve banks each have to put up one-half of the amount that is loaned. I do not believe that that was ever contemplated in the law. The \$139,000,000 of the surplus of the Federal Reserve Banks that was appropriated by Congress for capital of the Federal Deposit Insurance Corporation, it was expected, would be returned to the Federal Reserve Banks out of part of the gold profit, and there was set aside \$139,000,000 of the gold increment in the Treasury for the purpose of reimbursing the Reserve banks for the amount of the surplus that had been taken away. However, that was to be reimbursed to them only for the specific purpose of making these direct industrial loans.

The Treasury was given broad powers with reference to the appropriations, and they made a regulation that they would not appropriate any of this money except on a basis of dollar for dollar of what the Reserve banks put up. That in itself was a great deterrent, because with the surplus of the banks reduced by \$139,000,000, and the banks being required to put up part of what was remaining in loans, made them rather restrictive in the credit policy, in addition to complying with statutory restrictions. The requirement that they put up dollar for dollar with the \$139,000,000 fund naturally caused them possibly to be more restrictive than was contemplated or than they otherwise would have been.

Senator ADAMS. Mr. Eccles, so that I may get the chronology clear in my mind, the Federal Deposit Insurance Corporation law was passed prior to the gold devaluation? That is, the \$139,000,000 was put in out of the capital or the surplus of the Federal Reserve System into the Federal Deposit Insurance Corporation. That was one transaction in and of itself?

Mr. ECCLES. That is correct.

Senator ADAMS. When you refer to a restoration, that was a subsequent step not contemplated originally?

Mr. ECCLES. That is correct. It has the same effect as if it had been contemplated.

Senator WAGNER. Mr. Eccles, just so I might be clear on this, you are talking about dollar for dollar. Does that mean, for instance, that if a loan of \$100,000 was to be made, \$50,000 would be a commitment from the fund of \$139,000,000?

Mr. ECCLES. That is right.

Senator WAGNER. And the other \$50,000—

Mr. ECCLES (interposing). Would come out of the surplus of the bank. The proposed amendment, of course, changes that. The restrictions that have been referred to and exist in the present law would be eliminated in the amendments.

Senator CLARK of Idaho. How will this work with the present R. F. C. set-up? Will it parallel it if this amendment is passed and enacted into law?

Mr. ECCLES. Yes, it will.

Senator CLARK of Idaho. Will you get into a competitive situation there? For instance, suppose a loan was refused by the R. F. C. Would you dare commit yourself if they turned it down?

Mr. ECCLES. Well, we had, right from the beginning, a competitive situation.

Senator CLARK of Idaho. Yes; but you just did not make loans.

Mr. ECCLES. Well, we made the first 3 years more than the R. F. C. made, until they got their amendments. We both had a comparable situation.

Senator MEAD. You had a better record than they did.

Mr. ECCLES. I would prefer this not to be on the record.

Senator WAGNER (chairman of the subcommittee). Leave this off the record.

(A discussion was had which, at the direction of Senator Wagner, chairman of the subcommittee, was not recorded, and after which the following occurred:)

Senator DANAHER. I think that ought to be in the record, Mr. Chairman, and I have in mind that Mr. Jones himself testified before this very committee that the experience with these small loans was such that he expected the losses would be plenty—they were his words—and we will all recall that when the lending-spending bill was under consideration. I do not think there is any element of controversy between these two respective agencies. On the contrary, they should analyze for us and give us any expert opinion on a pending measure. I move that it be included in the record.

Senator CLARK of Idaho. Why don't you just submit the figures?

Senator WAGNER. I do not suppose he can put something in the record that is already off the record, unless he has an extraordinary memory of what he said.

Why don't you just submit the figures?

Mr. ECCLES. Can we not submit those figures, Mr. Smead? Yes. The figures are just a matter of record.

Senator WAGNER. Do not be quite so sensitive about your views. The other departments are not so sensitive about theirs.

Mr. ECCLES. I do not hesitate to express my views. I do not want to make it appear that there is any controversy between us, because, as I stated very frankly, as far as the Board or System is concerned, either Congress should repeal the present authority of the Federal Reserve bank or give us power and authority to really do a job; and we think, under the present circumstances, because of the extraordinary facilities we have, that we can do it, and there is no question that the R. F. C., with its greatly increased responsibility in specialized fields, will likely have a great deal to do.

The figures referred to above are as follows: From the passage of the act in June 1934, to January 31, 1935, when Congress first liberalized the R. F. C. authority to make these loans, the Federal Reserve banks had made loans and participations of thirty-two-million-odd dollars against approximately \$9,000,000 for the R. F. C. From January 31, 1935, until April 1938—when the bars were dropped again as to R. F. C. lending—i. e., 3½ years after the passage of the act, the accumulative figures show that the Federal Reserve banks had made loans and participations of one hundred and eleven-million-odd dollars, as against approximately \$105,000,000 for the R. F. C. The amendment of April 13, 1938, removed practically all restrictions on business loans by the R. F. C. From that date until the end of June 1939, the Federal Reserve banks continued to make new loans increasing the accumulative total of loans and participations by \$21,000,000. During this period the R. F. C.'s authorizations increased approximately \$235,000,000, although disbursements increased only about \$73,000,000. As of June 28, 1939, the Federal Reserve banks had authorized loans totaling one hundred and seventy-nine-million-odd dollars, of which \$14,000,000, or approximately 8 percent, had been canceled, whereas the R. F. C. had authorized a total of four hundred and thirty-four-million-odd dollars, of which \$85,000,000, or approximately 20 percent, had been canceled. None of the restrictions contained in the act authorizing the Federal Reserve banks to make these loans, as originally passed, have been removed.

The smaller lending up to, say, a million dollars as a maximum, can be decentralized and can be done through the Federal Reserve banks and the branches, and this fund which was set aside by Congress for this purpose—and only \$27,000,000 of it has been used—could be made effective and could be used.

There is this situation that may develop. Due to the preparedness program and the proportion that it is likely to reach and the period over which it may well extend, there are, no doubt, a great many small businesses that would be able to get contracts for the innumerable supplies in practically every field that the Government will require and they will need, no doubt, some capital.

The Government—at least, if you can judge by what happened in the last war—is often very slow in making payments, and we can expect that it may be as long as 6 months and in some cases a year before payments are made. That, I think, has happened in the past, and I do not believe that the larger businesses which are well financed

should have necessarily the great competitive advantage that they would have over many smaller businesses that may under the present circumstances not be well financed.

The smaller businesses, too, would very likely have difficulty going to a capital market. The cost involved in the changes that have been made in the elimination of the local underwriters, the bank security affiliates, and the registration requirements, has made the problem of capital financing to the small concern very much more difficult than was the case during former periods.

Senator CLARK of Idaho. You mean for capital loans?

Mr. ECCLES. That is right.

Senator CLARK of Idaho. As distinguished from working capital?

Mr. ECCLES. That is right. I am speaking of the longer term capital loans.

Senator HUGHES. What do you mean by the cost of the registration?

Mr. ECCLES. Well, I meant merely that there was certain accounting, certain inevitable costs, involved, and when it is charged against a small issue it makes it greater than if it is spread over a large issue.

Senator HUGHES. Yes; I realize that.

Senator CLARK of Idaho. Is your Board substantially of a uniform opinion, that is, perhaps not with everything you have said, but generally, as regards the ability of the Federal Reserve System to take over a broader field?

Mr. ECCLES. Well, I would say the Board would be unanimous in the view that the System could do this job. I would not want to say that the Board is unanimous in preferring the responsibility to do the job. I would say that a majority of the Board would be favorable—in fact, would like to have the responsibility to do this job. There is a letter from the Board stating the position of the Board on this question, so that the Board is on record as favoring this, but that was not the question you asked me.

The loans, as I started to say before we got a little off the question here, would be largely made, I think, by the member banks in each Federal Reserve area, the commitments for those loans being made by the Reserve banks.

For example, here is a concern to which a bank would not be willing to make a long-term loan on the terms required, but if the Reserve bank would say, "We will insure," which is in effect what a commitment means, or, "We will make a commitment to take up 90 percent of that loan at any time you desire us to do so, you carrying 10 percent of it, but on the 90 percent you will have to pay us 1 or 1½ or 2 percent, as the case may be, for the commitment," that is the way most of these loans are made, so that it is a question of the bank having the opportunity to make a credit that they now may not make.

Most of the loans that would be made would originate with the banks and they would merely use this broader facility of the Reserve System to enable them to make loans of this sort which at the present time, so far as making them through the Reserve System is concerned, they cannot make.

Now, a good many of them are being made through the R. F. C. Senator CLARK of Idaho. I do not want to unduly prolong this, but let me ask you this question. Would that create a situation

where the banks would tend to get all of their loans or more than usual insured? Might you not get into a situation where the Federal Reserve System would be substantially underwriting a greater part of bank loans?

Mr. ECCLES. No.

Senator CLARK of Idaho. You think not?

Mr. ECCLES. No.

Senator CLARK of Idaho. On account of that 1½ percent?

Mr. ECCLES. Very definitely. If a loan can be carried by a bank without a commitment, they are not going to have any desire to pay 1½ to 2 percent for that commitment. As a practical matter, the bank will carry all of the loans, if they feel that the risk is not too great, and to the extent that they feel it is greater than they want to carry, they may carry 20 percent, sometimes as high as 50 percent. On the border-line cases they may go only as far as 10 percent and take the lower rate and get the Reserve System or the R. F. C. to make the commitment.

Now, it works out, as a practical matter, very well, and as to the extent of lending that could be made, of course nobody can say, because looking to the future right at the moment, it is difficult to say how many of the small and middle-sized concerns, which are under-financed will get some of the Government and other business as a direct result of the Government preparedness program that is available.

In this connection—and this is a little aside from the question, but I think this may be a proper time to mention a matter that would be very helpful, and if there is no objection on the part of possibly the Treasury, which may have something to say about it, and I have not discussed the matter with them, because it is something that has come up very recently—there is the question of assignment of claims against the United States. May I just read a brief memorandum in that connection?

Senator WAGNER. Yes. May I ask you this question first? It is a very simple question. You spoke of long-term loans.

Mr. ECCLES. Yes.

Senator WAGNER. How many years would a long-term loan run?

Mr. ECCLES. Well, you may make a loan in which you require 50 percent, say, to be amortized over a period of 10 years—something like that—but I would not put limitations or restrictions on that. I think the question of the terms of the loan ought to be left discretionary. I would think, however, that 10 years would be the usual type of loan, and many of them shorter than that, but 10 years, I believe, would be the period of time that most borrowers would be satisfied with as a maximum.

Senator Mead has indicated that the proposed amendment is minor. The setting up of the Industrial Loan Corporation as provided in S. 2998 would, in my opinion, very much more adequately meet the situation. It would give the Board here power of initiation. The Reserve banks and branches would be used, of course. The loans would originate there and they would make the loans and they would service the loans as the agent for the proposed Industrial Loan Corporation, which would be a corporation under the Board.

There was the further provision that the Industrial Loan Corporation could issue debentures up to about three times or four times the capital that they had, so that if \$139,000,000 of capital which would be

available out of the gold profit was inadequate, they could raise additional funds for the purpose of carrying out a broader lending operation.

It has been indicated, however, that it is late in the session of Congress and it may be—

Senator WAGNER (interposing). It may be or it may not be.

Mr. ECCLES. That the proposed Industrial Loan Corporation bill would be difficult to take up at this time. I wanted to draw the distinction, however, between the broader powers and functions that would be given to the Board through the Industrial Loan Corporation and the proposed amendments.

Speaking of this question of assignment of claims, if claims could be assigned, there are, no doubt, many small and medium-sized concerns which would be able to get credit directly from their banks, possibly without using the commitments by the R. F. C. or the Federal Reserve, and there are others that would be able to get credit from the Federal Reserve with such an amendment as proposed that possibly could not even get it from the Federal Reserve under those conditions without being able to make an assignment. In other words, the ability to make assignments of claims for war orders would be of great assistance, I think—

Senator ADAMS (interposing). What do you mean by "war orders"?

Senator CLARK of Idaho. He means defense orders.

Mr. ECCLES. Defense orders; the war-preparedness program. As an important means of facilitating the Government's defense program, I wish to invite the attention of the committee to the desirability of removing the prohibition of the law upon the assignment of claims against the United States where those claims arise out of contracts with the Government providing for the production or the manufacture of materials and supplies necessary to the defense program.

Under the existing law, all assignments of claims upon the United States are void unless made in accordance with certain procedure after the claim has been allowed and a warrant issued for its payment.

I sympathize with the objective of this statute, which is the protection of the Government, and I am not proposing that it should be repealed or even modified except for a temporary period. I believe, however, that there may be many manufacturing or business concerns, particularly the smaller ones, who are not in a position financially to carry out a contract with the Government unless they can get credit by putting up the Government contract itself as security. If they were permitted to do this in cases where the materials to be furnished under the contract are a part of the Government's program, they would be enabled to borrow their necessary working capital from a bank or elsewhere by assigning their claim against the Government under a contract and then proceed to carry out the contract successfully. This obviously would be in the interest of the Government.

I feel that any such exception to the law, however, should be carefully limited, and I would suggest that it be restricted to a temporary period of, say, 3 or 4 years and be applied only to contracts with the Army and the Navy and the Procurement Division.

Moreover, in order to prevent the Government from being bothered with numerous very small assignments, I feel that a maximum amount of, say, \$3,000 should be placed upon assignments which would thus be recognized by the Government and that it be required that the entire amount of any such claim, and not merely a part interest therein, be assigned.

Senator DANAHER. You said "maximum." You mean minimum, do you not?

Mr. ECCLES. Minimum, that is right.

Senator DANAHER. Before you go on with that—

Mr. ECCLES (interposing). I finished that.

Senator DANAHER. We would require an amendment to this pending amendment even to cover that situation?

Mr. ECCLES. I am not suggesting that that be made in any part of this bill. It would seem that this possibly should be a separate matter, or it could be put in as an amendment to the proposed R. F. C. bill, which covers this large credit field.

I do not know what objection some other agency may have, but as a practical matter, I know that numerous bankers raised this question and there have been innumerable instances where the bankers have felt that such an amendment of this sort should be made.

Nothing has been done, and I would not raise it now under normal conditions, but we are thinking of ways and means of aiding these smaller concerns to bid, and not give larger concerns that are well financed an advantage in that respect. This sort of thing would help, without question, many concerns to make bids that otherwise could not do so.

Senator WAGNER. Have you that statute?

Mr. ECCLES. No. We could prepare one with a suggested amendment.

Senator HUGHES. There may be many people who make bids and secure contracts and then they might not be able to carry out those contracts.

Mr. ECCLES. Well, they could not carry out the contract unless they got financed.

Senator HUGHES. And then the bank would have to carry out the contract?

Mr. ECCLES. That is up to the bank. If a bank is going to be willing to extend the credit the bank is going to be pretty well satisfied that it is going to be able to carry it out.

Senator DANAHER. Will you look at subsection (a) of the pending bill and see if that is not an appropriate place to add a clause to cover this very thing?

Mr. ECCLES. Of course, this is a bill that has not passed the House at all. It occurred to me that if there is a definite assurance that this present R. F. C. bill that is pending or some other bill would be passed, something of this sort might be made as an amendment. This proposed bill has got to be taken up in the House and the question of tying something on to it would seem to me not to be so desirable, because this bill may not pass. We ought to try to get this sort of thing through now.

Senator HUGHES. It might be tied, as I understand it, on to some other bill?

Mr. ECCLES. Yes. Of course, it is up to Senator Mead. If Senator Mead would want to suggest this as part of this proposed bill, he might do that.

Senator MEAD. It recommends itself very highly to me, because I can see it is in the interest of the smaller businessman that we are trying, in this bill, to help. I would hope it would add strength to the possibilities of this bill. If it must be passed at this session it

probably would be better to tie it on to a bill that is already passed in both Houses.

Mr. ECCLES. The bankers would be very much in favor of this sort of bill.

Senator MEAD. So far as I am concerned, with regard to the pending bill, I will accept that as an added provision to Senate 3839.

Senator WAGNER. There must have been a reason for the prohibition in the statute. There must have been some abuses.

Mr. ECCLES. I suppose there were, and I can imagine there would be. What I am suggesting here is that there would be some limitations.

Senator WAGNER. What are the limitations?

Mr. ECCLES. Well, a minimum amount, for instance, and that the entire claim be assigned. If here is a concern that wants to divide the assignment up among 50 creditors, it would be a terrible situation, and you would not want the Government to have to accept a partial assignment, the idea being that a concern would get financed for the entire amount, and the Government under those conditions would simplify very much the handling of such an assignment.

Senator CLARK of Idaho. Well, under normal conditions, the Government does not like assignments bobbing up all over.

Mr. ECCLES. I don't blame them.

Senator CLARK of Idaho. They do not recognize attachments or garnishments.

Mr. ECCLES. This would be merely limited to the Navy, the Army, and the Procurement Division. It would not cover the whole field. Those are the limitations that I am suggesting.

I have not studied this particular question thoroughly and have not gone into what all the objections may be. I am looking at it purely from the standpoint of one means of helping concerns to get credit from banks, a means that does not now exist.

Senator CLARK of Idaho. Well, there might be some opposition, too. I can see where the General Accounting Office won't like it.

Mr. ECCLES. They won't like it.

Senator CLARK of Idaho. There may be things that arise in the performance of the contract that would reduce it and there might be some question with the banks, and I can see where the Comptroller might not like to have that.

Senator DANAHER. And that is the chief reason for the existence of 3477, because after the World War we had millions and millions of dollars in conflicting claims. We even had to set up a special board in the Department of Justice to handle them.

Mr. ECCLES. Inasmuch as we are talking about this question of credit, it occurred to me that this may be a good place to raise it at least for the consideration of this committee. I am not making a recommendation. I am not here proposing this, but I do think that it is something that the committee might well want to consider in connection with this whole subject.

Senator HUGHES. I think it is.

Mr. ECCLES. Mr. Chairman, I do not think of anything more to say on this subject. If there are any questions that any member of the committee would like to ask, I will be glad to try to answer them.

Senator WAGNER. Mr. Eccles, you said that you had really no recommendation to make, that it is up to Congress to decide this

question of policy, but I wanted to ask you a question with regard to that, because I know you are a student in many fields, but particularly in the economics field. Do you think it desirable at this time, perhaps because of the emergency which we all recognize now, that this sort of power supplementing what is being done by the R. F. C. is a very desirable proposal?

Mr. ECCLES. I think it is possibly more desirable now than it has ever been. I think that the use that the facilities of the Reserve System can be in this field is evident, and certainly it cannot be in any way harmful to the situation, and I can see that it may very well be helpful.

As I stated earlier, a great portion of the efforts and activities of the R. F. C. is likely to be in these large, specialized fields, and the Reserve banks and the branches would undertake to make the smaller loans largely through the member banks that they are in daily contact with in their community, and it is a natural relationship.

It does seem a rather unusual situation to expect a member bank, if it wants to get a commitment for a capital loan to a customer, to go down to the Federal Reserve bank and not see the Federal Reserve bank about it, but see the R. F. C. agency that is located in the Federal Reserve bank. That is what happens. Why not go directly to the Federal Reserve bank and get the commitment? Today the member bank goes to the Reserve bank, not to see the Reserve people, but to see the R. F. C. agency that is located in the Federal Reserve bank.

Senator HUGHES. Could it be extended to the nonmember bank also?

Mr. ECCLES. That is right. There is no limitation. I merely mentioned the member banks because about 85 percent of the deposits are in the member banks.

Senator HUGHES. There are many State banks.

Mr. ECCLES. The bigger State banks are member banks. This in no way would exclude any of the banks. Any bank could come in.

Senator WAGNER. There is the small borrower or the small businessman who has difficulty in securing loans, and I think the facilities for him ought to be increased.

Senator DANAHER. I had some correspondence with the Governor and he wrote me a splendid letter under date of May 28, 1940, in response to my letter. I wonder if you would mind putting that in the record?

Mr. ECCLES. You mean the letter I wrote in reply to your letter?

Senator DANAHER. Yes.

Mr. ECCLES. The opinions expressed in this letter are mine.

Senator DANAHER. I thought it was so good and so clear in explanation, Mr. Chairman, and I would be very happy to read that into the record.

Senator WAGNER. Very well.

Senator DANAHER. It is dated May 28, 1940, addressed to me:

I am in receipt of your letter of May 18, 1940, and its enclosures, in which you ask for any comments I may care to make with reference to Senator Mead's proposed amendment (S. 3839) to section 13b of the Federal Reserve Act.

Section 13b of the Federal Reserve Act now authorizes the Federal Reserve banks to make loans and advances with maturities not exceeding 5 years to estab-

lished industrial and commercial businesses in order to supply them with working capital. It also authorizes the Federal Reserve banks to participate with financing institutions in making such loans and to make commitments in connection therewith.

The requirements of the present law that such loans may be made only to provide working capital, only to established businesses, and only with maturities up to 5 years have made it impossible for the Federal Reserve banks to grant credit to many worthy business enterprises, particularly in cases where additional funds are needed for expansion or improvement. Senate bill S. 3839 would broaden the authority of the Federal Reserve banks in making industrial loans by eliminating these unnecessary restrictions. Similar restrictions, originally contained in the law under which the Reconstruction Finance Corporation makes advances to business enterprises, have been eliminated.

In addition to the above changes, S. 3839 would eliminate the industrial advisory committees, which are now required to pass upon applications for loans made under section 13b of the Federal Reserve Act. The bill would also direct, instead of merely authorize, the Secretary of the Treasury to pay to the Federal Reserve banks up to \$139,299,557 out of the increment resulting from the reduction in the weight of the gold dollar in order to enable them to make such loans. This would involve no additional appropriation of public funds or increase in the Budget, as the Secretary of the Treasury is already authorized to pay to the Federal Reserve banks all amounts which he would be directed to pay under this bill. Such amounts would be paid to the Federal Reserve banks from time to time, upon request by the Board of Governors of the Federal Reserve System, and in such amounts as the Board of Governors deemed necessary to enable the Federal Reserve banks to make the loans, advances, commitments, etc., authorized by the amendment. Senator Mead's proposed amendment would also increase from 80 to 90 percent the portion of any loss which might be assumed by a Federal Reserve bank on loans made by financing institutions in cooperation with or under commitments obtained from Federal Reserve banks.

It seems to me that the Federal Reserve banks can be most helpful to worthy business enterprises which cannot obtain credit on a reasonable basis from the usual sources, by encouraging banking institutions to make loans to them under the protection of commitments from the Reserve banks, for which fees are charged, obligating the Reserve banks to absorb an agreed portion, not in excess of 90 percent, of any losses that are sustained on the loans.

If the Federal Reserve banks are to do effective work in this field, they should not be required to turn down loans to business enterprises simply because the proceeds are to be used in part for plant rehabilitation or expansion or for any other reason except that the loans cannot be made on a reasonable and sound basis. Section 13b of the Federal Reserve Act, should, therefore, in my opinion, be amended along the lines of S. 3839.

Should Congress, however, be unwilling to amend section 13b as indicated or in any other way broaden the powers of the Federal Reserve System to provide credit in the field under discussion, it is my strong feeling that in fairness to the Federal Reserve, section 13b should be entirely repealed and the loans and commitments now outstanding under that section be gradually liquidated. So long as the section is in effect in its present restricted form the Federal Reserve banks suffer from the erroneous implication that they are not willing to extend this type of credit, whereas the greatly liberalized powers of the Reconstruction Finance Corporation in this field make it impossible for the Federal Reserve banks to make a comparable showing. My own preference is, of course, that the section be amended or that some other legislation be enacted to broaden the powers of the Federal Reserve System to provide such credit since the 12 Federal Reserve banks and their branches with experienced staffs in close contact with the business conditions and credit needs at all these points constitute an almost ideal field organization for carrying out the purposes Congress had in mind when section 13b was enacted. The desirability of such legislation is increased, it seems to me, in the present situation when many businesses might contribute substantially to the production of goods for the enlarged national-defense program provided adequate credit for fixed capital as well as for working capital is readily available.

The opinions expressed in this letter are my own and do not necessarily represent the views of any other member of the Board.

Sincerely yours,

MARRINER S. ECCLES, *Chairman.*

Senator WAGNER. I have received a letter from the Treasury Department with regard to this legislation, and it is rather lengthy I just want to read this so we might comment on it:

MY DEAR MR. CHAIRMAN: Further reference is made to your letters of February 14 and April 25, 1940, requesting an expression of the Treasury Department's opinion as to the merits of S. 3343 and S. 3839 to amend section 13b of the Federal Reserve Act, as amended. Inasmuch as S. 3839 differs only slightly from S. 3343, this report will relate to both bills.

Section 13b at present authorizes the Federal Reserve banks to make loans to, or purchase obligations of, established industrial or commercial businesses for the purpose of providing such businesses with working capital, the loans or obligations not to have a maturity exceeding 5 years. The proposed legislation would amend these provisions of section 13b to eliminate the requirements that the loans or obligations be made to established businesses, that they be made for the purpose of providing working capital and would also eliminate any requirement as to the maturity of such obligations. Section 13b at present authorizes the Federal Reserve banks to discount for, or purchase from, banks or other financial institutions obligations entered into for the purpose of providing working capital for established businesses provided that each such financing institution obligates itself for at least 20 percent of any loss sustained by the Federal Reserve bank upon any of the obligations so acquired from such institution.

The proposed legislation provides that the financing institution obligate itself for only 10 percent of any such loss sustained by the Federal Reserve bank. Loans heretofore made under section 13b have been made jointly with Treasury funds and funds of the Federal Reserve banks. The proposed legislation would amend section 13b to provide that the industrial loans by the Federal Reserve banks would be made only from amounts paid to the Federal Reserve banks by the Secretary of the Treasury under the section, except that when in the judgment of the Board of Governors of the Federal Reserve System, the amounts paid by the Secretary of the Treasury were inadequate for operations under the section, the Federal Reserve banks, with the approval of the Board, might continue operations through the utilization of their own funds until the amount of such funds so utilized equaled the amounts received by the banks from the Secretary of the Treasury. Payments heretofore made by the Secretary of the Treasury to any Federal Reserve bank under the provisions of section 13b would be subject only to the terms of the section as amended by the proposed legislation.

It is the view of the Treasury Department that if Federal Reserve banks are to continue to make industrial loans, as contemplated by the proposed legislation, they should be permitted to do so with their own funds and the Government should withdraw its funds heretofore advanced to the banks for this purpose and terminate the authorization for further advances. Under the proposed amendment to section 13b the Federal Reserve banks would make industrial loans principally from funds furnished by the Treasury. If Treasury funds are to be used for industrial loans consideration should be given to the question of whether such funds could be more effectively administered by an existing executive agency of the Government.

The maximum amount at present authorized by section 13b for advancement to the Federal Reserve banks is \$139,299,556.99, of which \$27,546,310.97 has been advanced. There has been no advance to any Federal Reserve bank under this authorization since October 1937. Total payments received by the Treasury from banks amount to \$345,842.05. A total of only \$24,578.66 was received by the Treasury from five banks, as a result of 1939 operations, under the 2-percent payment provision prescribed in section 13b.

Since June 1934 there has been over \$139,000,000 in the Treasury available upon call by the Federal Reserve banks but the maximum amount of loans outstanding at any time was only \$32,719,000, on October 30, 1935, and on February 21, 1940, only \$12,721,000 of loans were outstanding. The peak of outstanding commitments was \$28,002,000, on November 27, 1935, and they totaled only \$8,638,000, as of February 21, 1940. The gross amount of loans made by all Federal Reserve banks to December 31, 1939, was \$62,900,000 and repayments \$48,700,000, leaving a balance of \$14,200,000. Gross commitments to December 31, 1939, were \$70,200,000 and reductions and expirations were \$61,100,000, leaving a balance of \$9,100,000.

On the basis of the aggregate funds employed, both Treasury and Federal Reserve bank funds, gross earnings, expenses, losses and reserves for losses and current net earnings, as of December 31, 1939, were as follows:

Gross earnings.....		\$6, 817, 773. 77
Less: Expenses:		
Administrative.....	\$3, 605, 259. 35	
Expense for maintenance of miscellaneous assets acquired.....	36, 629. 84	
Losses charged off (other than those charged to reserves).....	416, 444. 75	
Losses charged to reserves.....	319, 308. 39	
Reserve for loss.....	2, 041, 528. 70	
		<u>6, 419, 171. 03</u>
Current net earnings.....		398, 602. 74

Section 13b of the Federal Reserve Act as it now exists contains a number of ambiguities and the Treasury Department has experienced considerable difficulty in arriving at any definite basis of agreement with the Board of Governors of the Federal Reserve System relative to the status of funds heretofore advanced by the Treasury, especially with respect to an acceptable formula for determining definitely the income derived from the use of funds advanced by the Treasury, and the bearing which profits and losses have upon the amount of funds subject to repayment by the banks. Consequently, the banks have been operating under arrangements promulgated by the Board of Governors of the Federal Reserve System but which have not been agreed to by the Treasury.

Certain provisions of section 13b, which provide for the payment to the United States of all dividends, all payments on liquidation, and all other proceeds of the stock of the Federal Deposit Insurance Corporation which has been pledged as security for advances to the Federal Reserve banks, are ineffectual because no dividends are now payable on stock of the Federal Deposit Insurance Corporation and there is little likelihood of repayments being available from the liquidation of such stock, as the Corporation has no limitation upon its life.

Other provisions of section 13b governing payments to the Treasury by the Federal Reserve banks provide as follows:

"Each Federal Reserve bank, in addition, shall agree that, in the event such dividends, payments, and other proceeds in any calendar year do not aggregate 2 per centum of the total payment made by the Secretary of the Treasury, under this section, it will pay to the United States in such year such further amount, if any, up to 2 per centum of the said total payment, as shall be covered by the net earnings of the bank for that year derived from the use of the sum so paid by the Secretary of the Treasury, and that for said amount so due the United States shall have a first claim against such earnings and stock, and further that it will continue such payments until the final liquidation of said stock by the Federal Deposit Insurance Corporation."

It is not clear from the above language whether the payments to the Treasury constitute payments of interest or payments upon the principal amounts advanced to the Federal Reserve banks. Heretofore, net earnings in the aggregate, after charging against earnings all expenses of the Federal Reserve banks incident to making industrial advances, as calculated on the basis adopted by the Federal Reserve banks, have not been sufficient to reimburse the Treasury up to the full 2 percent per year on the total payments to all banks.

The maximum amount of advances and loans under section 13b outstanding on a monthly basis, as of the last Wednesday of each month, was on November 27, 1935, when advances outstanding amounted to \$32,634,000 and commitments outstanding amounted to \$28,002,000, a total of \$60,636,000. Treasury advances to Federal Reserve banks on that date amounted to \$23,517,000 and, accordingly, the Federal Reserve banks had approximately \$37,000,000 of their own funds employed for this purpose. Subsequently, as loans and commitments were liquidated the Federal Reserve banks have withdrawn their funds and are treating the remaining loans and commitments outstanding as being financed entirely with funds received from the Treasury. Aggregate outstanding loans and commitments have been less than \$27,000,000 since the end of April 1939. As a result of this treatment of the account by the Federal Reserve banks, the losses on slow loans, which in many cases are now becoming unrealizable and subject to substantial losses, are being charged in a number of banks entirely as losses against funds advanced by the Treasury, notwithstanding the fact that when such loans were originally made there was a joint participation of Treasury and Federal Reserve bank funds.

The proposed legislation to amend section 13b would still leave ambiguities whereby ultimate losses from these joint transactions could be charged to the

funds advanced from the Treasury, and does not make any reference to prorating ultimate losses against the Federal Reserve banks' funds used. Section 13b as originally enacted contemplated the use of Treasury funds and Federal Reserve bank funds, and the arrangements made between the Treasury and the Federal Reserve banks in the latter part of 1934 were based upon a joint use of funds. It is believed, therefore, that any amendment of section 13b should clarify the statute so as to treat advances and commitments heretofore made as joint undertakings in which not more than 50 percent of the funds were Treasury funds and the balance Federal Reserve bank funds. Such an amendment might also provide that loans and commitments should be liquidated on the same basis, the earnings, expenses, and losses being apportioned on such basis. The balance of Treasury funds after liquidation and apportionment of earnings, etc. should be returned and covered into the Treasury as miscellaneous receipts.

There is transmitted herewith a draft of a proposed amendment to section 13b which provides for the discontinuance of further advances from the Treasury, repayment of advances heretofore made, and a clarification of ambiguities now existing in the operation of the section.

If it is determined as a matter of policy to authorize the Federal Reserve banks to continue to make industrial loans with Treasury funds, and for the Government to assume all expenses and losses, and receive all net earnings, if any, on such loans, it is suggested that only the balance of the amount originally available, namely, approximately \$112,000,000, be used for new loans made after the effective date of the amendatory act. Industrial loans and commitments now outstanding should be liquidated on such a basis that losses and earnings would be shared jointly by the Federal Reserve banks and the Treasury, as set forth above.

Due to your request for expedition, the Department has not been able to secure advice from the Bureau of the Budget as to the relationship of the proposed legislation to the program of the President.

Very truly yours,

D. W. BELL,
Acting Secretary of the Treasury.

Senator DANAHER. Does that not suggest one question, after all? What effect would the adoption of 13b as amended have on outstanding loans and commitments?

Mr. ECCLES. Well, my understanding of that was that the \$27,000,000 that has been turned over to the Reserve System and has been loaned would be a portion of this entire fund. Now, I do not know that there would be any particular objection to that. In other words, we can take \$111,000,000 of new loans, and as these loans are liquidated the loss and expense would be prorated based upon the participation of the Reserve banks and the Treasury.

Does the present bill contemplate that, Mr. Vest?

Mr. VEST. It contemplates that the amount that is not paid shall be paid over.

Mr. ECCLES. As far as the \$27,000,000 is concerned, the losses on those loans and the expenses would be prorated and the income from the loans would be prorated on a 50-50 basis and would be separate and apart from the use of the \$111,000,000.

Senator DANAHER. Could not we fix it so we started with a clean slate on this new proposition, because they were written on a narrower basis?

Mr. ECCLES. With regard to these loans that are liquidated, instead of returning the \$27,000,000 to the Treasury, we should be permitted, it seems to me, to add it to the fund of the \$112,000,000. That is what was contemplated, instead of returning it to the Treasury at all. We will assume that we have received from the Treasury \$27,000,000, and as those loans are liquidated the losses upon those loans and expenses would be absorbed out of the \$27,000,000, and what may be

left of the \$27,000,000 would then be added to the \$112,000,000 and would be used as a revolving fund.

Senator DANAHER. Governor, would you examine the bill and see if it covers that, and, if it does not, would you send us suggested changes?

Mr. ECCLES. Isn't that the way it would work?

Mr. VEST. That is the way it would work.

Mr. ECCLES. And according to our present understanding of their proposal, there is no point in the question they raise.

Mr. SMEAD. To clear up the situation, we have never had a definite agreement with the Treasury on accounting procedure and who is to sustain the losses. We now have less loans and commitments outstanding than we have money from the Treasury. Presumably the Treasury would sustain any losses, but we never have reached a definite agreement.

Mr. ECCLES. Isn't this what we have done? We have taken the interest on the loans; we have kept a detailed record of the expense of making the loans; we have taken that expense plus the losses on the loans; and then we have taken those two items and deducted from them the earnings. If the interest collected is in excess of the losses, then, of course, there is something left over, and we have paid one-half of what is left over to the Treasury, up to 2 percent. If we did not get 2 percent, we would not pay them that.

Senator DANAHER. Governor, would you say that the language on page 5, starting on line 3, with the word "whenever" applies?

Mr. ECCLES. If there is any question about it, it seems to me we would have no difficulty working out a clarification of the thing that should be satisfactory to all concerned. I would like to see, Mr. Chairman, any amendment that the Treasury may propose with reference to it.

Senator WAGNER. It is in the letter that I read.

Mr. ECCLES. May we have a copy?

Senator WAGNER. Yes, and I will ask that this be inserted in the record at this point.

(The document referred to is as follows:)

A BILL To amend section 13b of the Federal Reserve Act, as amended

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 13b of the Federal Reserve Act, as amended, is amended by adding at the end thereof the following new subsection:

"(f) On and after July 1, 1940, no further payments shall be made by the Secretary of the Treasury to any Federal Reserve bank under subsection (e) of this section, and payments made prior to July 1, 1940, with the exception of those amounts of such payments directed to be returned to the Treasury pursuant to the third sentence of this subsection, shall be returned and covered into the Treasury as miscellaneous receipts as rapidly as loans, discounts, advances, purchases, and commitments outstanding under this section on July 1, 1940 are liquidated. For the purpose of adjusting the accounts of the respective Federal Reserve banks and the Treasury Department covering payments by the Secretary of the Treasury under this section subsequent to June 19, 1934, and for determining the amount to be returned to the Treasury, not in excess of 50 per centum of the aggregate amount of all loans, discounts, advances, purchases, and commitments outstanding under this section at any time shall be considered to represent funds advanced by the Secretary of the Treasury, and the balance of the aggregate amount of such loans, discounts, advances, purchases, and commitments shall be considered to represent funds of the respective Federal Reserve banks. The aggregate of all payments made by the Secretary of the Treasury to any Federal Reserve bank under this section in excess of 50 per centum of the total

amount of loans, discounts, advances, purchases, and commitments by such bank under this section outstanding on July 1, 1940, and all other amounts paid under this section to such bank by the Secretary of the Treasury which, on July 1, 1940, are not employed for loans, discounts, advances, purchases, or commitments under this section, shall be returned to the Treasury within six months after July 1, 1940, and shall be covered into the Treasury as miscellaneous receipts. The amount to be returned to the Treasury by each Federal Reserve bank shall be reduced by the total amount paid to the Treasury by such bank pursuant to subsection (e) of this section. All earnings, expenses and losses on the loans, discounts, advances, purchases, and commitments of each Federal Reserve bank under this section shall be prorated between the funds paid to such bank by the Secretary of the Treasury and the funds of such bank, on the basis of the amounts of the respective funds so employed, but in no event shall more than 50 per centum of the total earnings, expenses, or losses of any Federal Reserve bank be prorated to the funds paid to such bank by the Secretary of the Treasury. This proration of earnings, expenses, and losses shall operate to increase or reduce, as the case may be, the total amount to be repaid to the Treasury by each Federal Reserve bank. Upon repayment to the Treasury by any Federal Reserve bank of the total amount directed to be repaid by such bank under this subsection, the agreement executed by such bank pursuant to subsection (e) of this section shall be terminated *ipso facto*, and the stock of the Federal Deposit Insurance Corporation owned by such bank shall no longer be pledged as security for the amount paid to such bank by the Secretary of the Treasury. The Secretary of the Treasury shall have the power to make such rules and regulations as he may deem necessary for the administration of the provisions of this subsection."

Senator WAGNER. We will take an adjournment until Friday.

(Thereupon, at 12:10 p. m., an adjournment was taken until Friday, June 14, 1940, at 10:30 a. m.)

BUSINESS LOANS BY FEDERAL RESERVE BANKS

FRIDAY, JUNE 14, 1940

UNITED STATES SENATE,
SUBCOMMITTEE ON RECONSTRUCTION FINANCE
CORPORATION MATTERS OF THE COMMITTEE
ON BANKING AND CURRENCY,
Washington, D. C.

The subcommittee met at 10:30 a. m., pursuant to adjournment, in room 301, Senate Office Building, Senator Robert F. Wagner, presiding.

Present: Senators Wagner (chairman of the subcommittee), Adams, Hughes, Clark of Idaho, and Townsend.

Present also: Senators Danaher and Mead.

Senator WAGNER. The subcommittee will come to order. Mr. Wiggins, did you wish to say something on this subject?

Mr. WIGGINS. Yes, sir.

Senator WAGNER. Can you tell us now?

Mr. WIGGINS. Yes, sir.

STATEMENT OF A. L. M. WIGGINS, PRESIDENT, BANK OF HARTSVILLE, HARTSVILLE, S. C.; CHAIRMAN OF THE COMMITTEE ON FEDERAL LEGISLATION OF THE AMERICAN BANKERS ASSOCIATION

Senator WAGNER. You represent the American Bankers Association?

Mr. WIGGINS. Yes, Mr. Chairman. I am president of the Bank of Hartsville, at Hartsville, S. C., and am chairman of the committee on Federal legislation of the American Bankers Association.

Mr. Chairman, I wish to comment on Senate bill 3839, under which it is proposed that the powers of the Federal Reserve banks be expanded; and I wish to say that we neither oppose nor favor the measure, but we do wish to comment on it and to bring to the committee certain facts that we think make some contribution to the problems involved in the proposal before the committee.

There apparently is provided in the bill a provision to expand the present powers under section 13b, for the Federal Reserve banks to make industrial and commercial loans.

As to the provisions relating to the use of the Treasury funds or Federal Reserve funds, we have no comment at all to make; we think that is entirely a matter for Government agencies and for Congress. However, we are struck with the fact that, according to the testimony of Chairman Eccles and the report from the Treasury Department, both of these agencies seem to want the funds of the other agency

used for the purpose of making these loans. It seems to us somewhat significant that apparently neither of the agencies wants its own money used in making these loans—according to the letter which was filed with your committee earlier in the week, and the testimony of Mr Eccles.

I think there is general agreement that the conclusion that follows from Mr. Eccles' testimony is that the Federal Reserve banks have not done any considerable job in making loans to industry under the powers they now have. The report of the Federal Reserve System—the Federal Reserve Bulletin—shows that as of December 31, 1939, the total of the industrial advances of the Federal Reserve banks, outstanding at that time, was only \$13,683,000.

Senator DANAHER. Is that under the existing section 13b?

Mr. WIGGINS. Yes.

Senator DANAHER. Thank you.

Mr. WIGGINS. Yes, that amount of advances of Federal Reserve banks, outstanding at that time, was \$13,683,000. Naturally we can assume that if the powers are expanded, there will be more loans made; but we point so the fact that that is the total amount of loans outstanding as of December 31, 1939.

It is very difficult, from the form in which the reports are made by the Government agencies, to find out exactly what they are doing; but by using some mathematics we find that the number of loans they made, according to the reports contained in the Federal Reserve Bulletin, for the full year 1939 total 128, for a total amount of \$13,209,000. That represents the loans made during 1939, according to calculations, subtractions of totals outstanding, as shown in the Federal Reserve Bulletin. In other words, it has not been any important factor in the volume of credits extended up to this point.

Senator WAGNER. Is not that because of the limitation in the law itself?

Mr. WIGGINS. Mr. Chairman, I am going ahead to comment briefly on the Reconstruction Finance Corporation, which does not have the limitations, and I should like to undertake to develop what they are doing.

According to this same Federal Reserve Bulletin, the total loans outstanding made by the Reconstruction Finance Corporation to industrial and commercial business, as of the end of December 1939, was \$130,625,000. That is, according to the report of the Federal Reserve Bulletin. We have undertaken to find out how many loans the Reconstruction Finance Corporation actually made during 1939, but we have not been successful in determining that. None of the reports that we have been able to obtain carried that information. We made a request of the Reconstruction Finance Corporation for the information as to the amount of loans—number and amount—during 1939, for industrial and commercial banks; and they told us they did not have that in such form that it could be given to us; but we felt that that would be an important fact in the situation of knowing what has actually been done and what is actually being done.

I do not want the committee to get the impression that I am either criticizing the Federal Reserve banks or the Reconstruction Finance Corporation for what they have done or have not done. I am merely trying to get the facts with respect to what credit has been extended under the powers that they have. I think all of us agree that both

of these agencies have been diligent and constructive in their efforts to make these loans. I know that is true, from personal experience with the Reconstruction Finance Corporation. I have been on the R. F. C.'s advisory committee, down in our section of the country, since it was first established; and the R. F. C.'s relatively small amount of loans is not due, in my opinion, in any sense to any lack of diligence or effort on their part to make these loans.

Senator WAGNER. How many did you reject? I suppose you acted in an advisory capacity?

Mr. WIGGINS. Yes, sir.

Senator WAGNER. What percentage of the loans applied for did you reject, so far as you remember?

Mr. WIGGINS. Mr. Chairman, I could not give you that with any degree of accuracy. I will say that the loans rejected, as I recall them, have been in greater degree in recent years than they were in the earlier years. The average quality of loan applied for, from the credit standpoint, has not been as good recently as it was earlier; so that I believe our records would show that a larger percentage of loans has been rejected recently than in former years.

Senator WAGNER. Just so that I might be informed: You are a banker in your community, are you not?

Mr. WIGGINS. Yes, sir; I am president of a small country bank in South Carolina.

Senator WAGNER. Yes. These applications do not come to the Reconstruction Finance Corporation unless the applicant showed, in the normal course of business, that he was unable to secure the loan from a bank?

Mr. WIGGINS. That is correct, sir.

Senator WAGNER. So that as a member of the banking fraternity, having refused this loan, you then also act as an adviser to the Reconstruction Finance Corporation, to give advice with respect to whether or not, nevertheless, that loan should be granted by the Reconstruction Finance Corporation?

Mr. WIGGINS. That is true.

Senator WAGNER. Is there not a little conflict in that?

Mr. WIGGINS. Possibly so, to the extent that a banker who has refused a loan from his own funds might be inclined also to reject the loan—as a member of an advisory committee—no matter whose funds he represented.

Senator WAGNER. Yes; or he might like to see his position sustained by the advisory committee, too?

Mr. WIGGINS. Yes.

On the other hand, the temptation is on the other side in some cases, whereby the bank would like to see some customer get money that the banker, himself, is not willing to loan.

Senator DANAHY. Particularly if he can bail out the bank, in part?

Mr. WIGGINS. Of course, many of these loans are made in cooperation between the banks and the Reconstruction Finance Corporation, in participation.

Senator WAGNER. Yes; I know of that type.

Mr. WIGGINS. Yes.

Senator WAGNER. But usually in the smaller loans there is no type of participation.

Mr. WIGGINS. Yes, sir; generally speaking, that is true.

Senator WAGNER. I just wondered whether there was not a little conflict there.

Mr. WIGGINS. I might say that the Reconstruction Finance Corporation disregards the recommendations of its advisory committee whenever it sees fit to do so. It takes it for what it is worth, and then acts on its own judgment; and we have some cases in which the Reconstruction Finance Corporation has made the loan, where the advisory committee thought it was not a sound loan.

Senator WAGNER. The reason I asked that is not to be critical but, rather, because I wanted to be informed.

I am sure that one of the reasons that prompted the introduction of this legislation by my colleague, who has been interested in this matter for a long time, is because many persons have not been able to obtain these small loans from the banks; and, so, if the banker, who refuses to make the loan himself, acts in an advisory capacity for the R. F. C., I do not see how it changes the situation any.

Mr. WIGGINS. Yes. As a matter of fact, of course, it is seldom that a banker who has dealt with the applicant in his own bank, passes on the loan when it gets to the R. F. C. It is a voluntary service, as you know, and a large advisory committee is set up, and three members of the whole committee are required to pass on each application; and it is rather rare that the same banker who may have refused a loan to the particular applicant is also on the advisory committee of the R. F. C. that passes on the loan there.

Senator DANAHER. May I ask a question, Mr. Chairman?

Senator WAGNER. Certainly.

Senator DANAHER. Had you finished your comment on that particular approach to this matter? Because if you have, I have a specific question I want to ask your judgment on.

Mr. WIGGINS. I should like to make this point; that in spite of these facilities—limited as they may have been in the case of the Federal Reserve banks—there has not been any comparatively large amount of loans made, in terms of the credit requirements of this country.

In that connection I want to give you some figures on what has been done during 1939 in credit extensions by banks. These figures are available this morning for the first time, and they are based on an actual survey by the American Bankers Association, by means of a questionnaire sent to all the banks of the country. Forty-four percent in number of the banks responded with the information, and that 44 percent in number represents 75 percent of the deposits and approximately the same percentage of the banking resources of the country. So the figures we give you are from the 44 percent in number and approximately nearer two-thirds in resources.

Whereas the industrial advances of the Federal Reserve banks at the end of December 31, 1939, were \$13,683,000 and the outstanding loans of the Reconstruction Finance Corporation, as of the same date, were \$130,625,000, the outstanding loans of all the banks in the country—this is statistical—from this report, were \$22,167,000,000. In other words, the total outstanding loans of these two agencies in this field were only two-thirds of one percent of the total amount of loans outstanding, of all the banks.

Senator DANAHER. Loans outstanding are commercial loans?

Mr. WIGGINS. No; all the loans of the banks.

Senator DANAHER. Of whatever kind?

Mr. WIGGINS. Of whatever kind.

Senator DANAHER. Even on mortgages?

Mr. WIGGINS. Even on mortgages.

Senator DANAHER. All the loans of the banks?

Mr. WIGGINS. All the loans of the banks—credit extensions. Those figures are not broken down; it is a total figure.

Senator DANAHER. Very well.

Mr. WIGGINS. Now, Senators, the significant fact, and the one in connection with which I am sorry I do not have the R. F. C. figures of loans made in 1939, is this: Whereas, the total of the industrial advances of the Federal Reserve banks is a total of 128, of an aggregate amount of \$13,209,000, during the same period of 12 months the 44 percent in number of the banks, representing two-thirds of the banking resources, actually made during the same period new loans—not renewals, but new loans—totaling 12,675,000 in number, or a total amount of \$23,115,000,000.

Senator HUGHES. How many loans was that?

Mr. WIGGINS. 12,675,000 in new loans.

Senator ADAMS. And the Federal Reserve made 128?

Mr. WIGGINS. Yes, sir.

Senator WAGNER. Those 12,675,000 new loans represent how much money?

Mr. WIGGINS. Representing \$23,115,000,000. Now, gentlemen, they are actual figures obtained from the records of the banks of the country, through a questionnaire; and they represent only two-thirds of the banking resources—from which we have been able to get this data.

There are other significant figures obtained from this questionnaire: Of these new loans, there were made during the last 6 months of the year, as compared with the first 6 months—and I think there is some significance in the changes—in the last 6 months of 1939, these 44 percent in number of banks made 6,643,000 of these new loans, in an amount of \$12,592,300,000. In addition to that, during that same period they renewed 6,106,000 loans, in an aggregate amount of \$7,835,600,000. In other words, they made more new loans, in an amount of more than 50 percent greater than the dollar volume of the loans renewed.

Now, Senators, those figures will astonish many people who have questioned whether or not banks are lending money.

I should like to call your attention also to the fact that included in these new loans made by banks there were 285,000 new mortgage loans, in an aggregate amount of \$899,600,000.

I also call your attention to the fact that many banks, particularly the larger banks, have outstanding what they call lines of credit to business; and a survey for the first 6 months of 1939 showed that only 27 percent of the lines of credit outstanding were being used. For the last 6 months of the year the reports show that 33 percent of the lines of credit outstanding, for banks, are being used. Of the total outstanding lines of credit of \$5,507,000,000 to business, there was actually being used of that \$1,817,000,000. A great deal has been said about loans to small business, and so forth; and of course I know that average figures do not necessarily mean a great deal; but we have broken this down into averages; and we find that the average size of new loans made during the last half of 1939 was

\$1,896; the average size of all of the new loans made during the last 6 months was less than \$2,000.

The average size of loans renewed was \$1,283. The average new mortgage loans are \$3,091. I give you those figures to show that, relatively, the operation of banks is in the field of small loans.

Senator CLARK of Idaho. May I inquire, Mr. Chairman?

Senator WAGNER. Certainly.

Senator CLARK of Idaho. I suppose that a large percentage of loans—both those outstanding and those that have been made—are what might be called turn-over or inventory loans—that is, short-term commercial paper? In other words, eliminating the mortgage loans, of course, which are in a class entirely by themselves, I suppose, I am just asking you, really, if the great bulk of those are probably 90-day or 120-day paper or perhaps up to a year?

Mr. WIGGINS. May I answer that by saying that a great deal of it is short-term; but I should like to call your attention in connection with that question to a survey made by the Board of Governors of the Federal Reserve System, about a year ago, which shows that on April 19, 1939, reports from 400 banks—and I assume they are the larger banks—but from approximately 400 banks, a survey showed that they had outstanding at that time 24,900 intermediate-term loans, aggregating \$1,420,000,000.

Senator CLARK of Idaho. \$1,420,000,000?

Mr. WIGGINS. Yes; \$1,420,000,000, from these 400 banks.

Senator CLARK of Idaho. What would be the term? What would the term of those loans average?

Mr. WIGGINS. Most of the term loans run from 3 years to 5 years, and some run from 6 years on up to 10 years. Many of the banks have gone into 10-year-term loans.

Senator CLARK of Idaho. Would you consider those capital loans?

Mr. WIGGINS. In many cases they are. In many cases they are loans to replace working capital which has been lost. They use the longer term in order to permit them, out of earnings, to repay over a period of time.

Senator CLARK of Idaho. Would you consider many of those loans what might be termed "risk capital"?

Mr. WIGGINS. Necessarily, bank loans cannot be used very largely in the risk-capital field.

Senator CLARK of Idaho. That is my thought; yes.

Senator TOWNSEND. There might be a risk there, but you would not want to use the word? Is that correct?

Mr. WIGGINS. Yes; there is risk.

Senator TOWNSEND. I am sure there is some risk there.

Mr. WIGGINS. Yes, there is risk.

Senator WAGNER. They are not what you call "venture loans," are they?

Mr. WIGGINS. Well, of course, Mr. Chairman, every loan has in it some element of risk, and that is where the element of judgment comes in; but when you are lending money on a term loan, at 3½ or 4 or 5 percent, naturally you must reduce your risk to a minimum.

In that connection, Senator, may I call your attention to this fact: Of these 24,900 intermediate-term loans, aggregating \$1,420,000,000, 92 percent of them were loans of \$100,000 or less; 92 percent of the term loans in the 400 banks were in amounts of \$100,000 or less. I

bring that out because of the considerable discussion we have had about small loans.

So I bring these figures and these facts before this committee not in any way to disparage the efforts of the governmental agencies that have been attempting to supply a field and a particular credit requirement, but for the purpose of calling to your attention, to bring out as forcefully as I may, the fact that it is almost insignificant, in terms of the total credit needs of business and industry of the country, as supplied by the chartered banking institutions of the United States.

Senator TOWNSEND. Do you have in your statement there, anywhere, a break-down of the number of loans applied for and turned down, and the amounts?

Mr. WIGGINS. By the chartered banks?

Senator TOWNSEND. Yes.

Mr. WIGGINS. Senator, we are working that up. It has been rather difficult to get adequate data on that particular subject; because many banks do not keep such records.

Senator TOWNSEND. I know that is true.

Mr. WIGGINS. But we now have more banks—at our urgent request—keeping those records; and as soon as we are able to accumulate enough to really mean anything, we hope to have an opportunity to present the figures to this committee.

Senator TOWNSEND. Are you a banker?

Mr. WIGGINS. Yes, sir; I am president of a small country bank.

Senator TOWNSEND. From your experience as a banker, you would not expect to find a very great percent of loans that were applied for and not granted, would you?

Mr. WIGGINS. It is a rare case, today, when a banker turns a loan down. I will give you a personal illustration from our own institution, of what I think is rather typical today: We had a case of a man who needed some money. He lived about 40 miles away; he was running a little meat business. He had been fairly successful, and he needed \$2,000 to buy some more equipment to extend his little meat business. When he applied for a loan to us, with a statement, the loan could not be made. He did not have a statement that would justify it. But we sent a man 40 miles away to this little town, and he spent 2 or 3 hours here, finding out if there was any way that we could work out a loan for this man. It wound up by our having to take a little insurance policy and a claim on a couple of trucks and a chattel mortgage on some machinery; but the net result was that we worked out a loan for this man and made him the loan of \$2,000, and spread it over a period of 3 years, so that he could pay it out of the earnings of that little business.

I mention that because I think it is typical of what banks are doing today.

Senator TOWNSEND. I think it is. I happen to be president of a little bank, and I am also a director of a bank in the State; and my colleague is also a stockholder and director. I know from my own experience that just those things happen, and we do try to make every loan that is applied for, in any way possible to feel secure.

Mr. WIGGINS. In our own bank I would say that we make 95 percent of the loans applied for—certainly, not on the original basis applied for in every case; but we make the loan if we can—and it is not because we are Good Samaritans; it is because we have surplus

funds that we cannot make a profit on. Half of our funds are cash that we want to invest, and if we invest it we make more income.

Of course, I do not want to create the impression that the bankers have suddenly become Good Samaritans. It is common sense that they make the loans if loans can be had, that are reasonably safe.

I would also like to call attention to one other fact, Mr. Chairman; and I think it is very heartening in these most tragic times: that the chartered banks of this country have never had greater deposits than at the present time. In my opinion they have never been in a sounder financial condition; and, also, at the present time they have the staggering total of excess reserves, according to the report in the morning paper, of \$6,610,000,000; and whatever the demands of this country and no matter how great the credit requirements may be in this emergency which seems to lie ahead, the chartered banking system is able, has the resources, has the attitude, has the interest and the desire adequately to serve the credit needs of business and industry in this country.

I call your further attention to the fact that this excess reserve of \$6,610,000,000 will support additional credits of more than \$40,000,000,000. It is amazing that the excess reserves of the banking system of this country are adequate to make loans aggregating almost the entire national debt; and I say that, to me, that is a heartening situation for us to meet during these trying times.

Senator CLARK of Idaho. I would like to get your opinion on this. It is a little collateral, but it has been suggested to the committee that certain small and intermediate businesses obtaining contracts from the Government for what may be called defense orders have been unable adequately to finance themselves or finance these contracts because the Government does not pay very promptly sometimes, and under the existing law, contracts with the Government cannot be assigned to a bank for purposes of credit.

It has been suggested that for a brief period of time, more or less in the nature of an emergency, that statute be modified to permit the assignment of contracts with the Government—War Department and Navy Department—to banks for purposes of credit. The purpose, of course, would be to enable a small and sound business to compete in a measure with the great corporations in obtaining Government contracts.

Here is some suggested language. I would like to get your views on it. You seem to have a rather remarkable grasp of this whole situation:

In any case in which the entire amount of a claim upon the United States of \$3,000 or more based upon a contract entered into on behalf of the United States by the War Department, Navy Department, or the Procurement Division of the Treasury Department is transferred or assigned to a bank or other lending agency as security for a loan or credit, the proceeds of which are to be used to finance the performance of the contract with the United States upon which such claim is based, such transfer or assignment, if otherwise valid, shall not be rendered invalid with regard to the United States or any other person by the fact that the claim is one upon the United States, notwithstanding any other provision of law.

The provisions of this paragraph shall be effective until the expiration of a period of 4 years from the enactment of this act.

Would you think that would be of some assistance to business in general, particularly to small and intermediate business?

Mr. WIGGINS. I should think it would. In a facility that increases the usability of a business' credit resources—and a credit is a re-

source—it would seem to me to be of value to that business in obtaining credit.

Now, as to the proposal, there are so many administrative problems involved from the standpoint of the Government that I am not quite sure how practical the thing might be in operation; but answering your question as to its desirability, from the standpoint of giving a business an additional credit resource that can be used, I think it unquestionably would be.

Mr. Chairman, if I may be permitted to do so, the figures have just been handed me, which have been dug out from four quarterly reports of the R. F. C., which would supplement the statement which I originally made, and the figures show that authorizations of loans by the Reconstruction Finance Corporation to industrial and commercial business during the year 1939 aggregated 1,689, in a total amount of \$124,379,563.

That compares with the figure that I gave you of 128 loans made by the Federal Reserve banks, totaling \$13,209,000, and 12,675,000 loans were made by banks, in a total amount of \$23,115,000.

Senator TOWNSEND. Your statement covers only the Federal Reserve banks, is that correct?

Mr. WIGGINS. My last statement as to banks covers all banks, Senator.

Senator TOWNSEND. Covers all banks?

Mr. WIGGINS. Covers all banks.

Senator DANAHER. May I ask you a question as to your judgment with reference to the elimination of the requirement that 2 percent be paid out of earnings?

Mr. WIGGINS. As proposed in this bill?

Senator DANAHER. Yes; this bill would eliminate that.

Mr. WIGGINS. I think, Senator, it is largely a matter of to whom he is going to furnish the money and who is going to take the losses. As between the Federal Reserve banks and the Treasury Department, it is a matter of deciding who is to get any income or take any losses.

Senator DANAHER. If we left the requirement in that the 2 percent be paid, if earned, it probably would facilitate negotiating some adjustment there, would it not, if it had to be done?

Mr. WIGGINS. Frankly, I would prefer not to comment on the question that seems to be involved between the Treasury and the Federal Reserve System. Evidently there is something in that picture that needs consideration.

Senator DANAHER. All right. There is one other question I have. This bill, on page 2, starting with line 13, reads:

Each such financing institution shall obligate itself to the satisfaction of the Federal Reserve bank for at least 10 percent of any loss which may be sustained by such bank—

and so forth.

Now, under the present section 13 b, the percentage of participation it must bear is at least 20 percent of any loss that may be sustained. Do you think that the relaxation of that proportion is called for under present exigencies?

Mr. WIGGINS. Do I get your question to mean whether or not it is desirable to reduce the desired participation from 20 to 10?

Senator DANAHER. That is right.

Mr. WIGGINS. I do not believe that would have any material effect one way or another. Some banks might be willing to take 10 percent of a loan who might not be willing to take 20 percent, and there might be some additional participation as a result of that.

Senator DANAHER. It would not be great, in any case?

Mr. WIGGINS. I should not think so. It would seem to me that a bank that would not be willing to take 20-percent participation in a loan would not want to fool with 10 percent, but there might be some cases; no doubt, there would be.

Senator ADAMS. Mr. Chairman, I did not mean to interrupt, but there were two or three figures that I think might be added to the accumulation. I am looking at the Federal Reserve Bulletin of June 1940, and it may be of interest.

The total number of banks in the United States is 15,035.

The total amount of deposits is \$58,344,000,000.

The total amount of loans and investments in all the banks was \$50,883,000,000.

The total amount of loans was \$22,167,000,000.

The total amount of investments was \$28,000,714,000.

Mr. WIGGINS. Mr. Chairman, if I may be permitted to make one further point—we are talking about small business—I might say that the banks are a small business, very largely. Of the 15,000 banks in this country today, 12,000 of them have deposits of less than \$2,000,000, approximately 85 percent, and they employ an average of 3 officers and 11 employees.

The average officer's salary in the banks of the United States is less than \$3,500 for all of the bank officers in the United States, and if you omit the large metropolitan centers, the figure, of course, is much less.

Senator TOWNSEND. That is the average of all banks?

Mr. WIGGINS. Of all bank officers in the United States; it is under \$3,500.

Senator TOWNSEND. That is a great surprise to me.

Mr. WIGGINS. And I would like to make a further point showing that banks are a small business. Of the national banks of the United States, 75 percent of them pay annual dividends of \$5,000 or less, and over half of them pay annual dividends of \$3,000 or less. So when we talk about small business and small loans and loans to small business, that is the field that the vast majority of the banks themselves are in, because they are a small business.

Senator CLARK of Idaho. Of course, that is true, and there have been times when we have had to find extraordinary methods of helping that type of small business through Government agencies.

Mr. WIGGINS. That is right.

Senator CLARK of Idaho. Those times, we know, are past now—at least, for the present.

Senator TOWNSEND. We are doing some of it now.

Senator CLARK of Idaho. Some capital rehabilitation is being done by the R. F. C. in banks?

Senator TOWNSEND. Oh, yes.

Mr. WIGGINS. I would like to point out the fact that the advances by the R. F. C. to banks have been a most profitable operation to the Government financially and the loans are being repaid with interest.

Senator CLARK of Idaho. I think there is no question about that, but I was merely calling attention to the fact that frequently all types of small business, including banks, may have, in certain instances, to draw upon the credit resources of the Federal Government.

Senator ADAMS. As a matter of fact, banks are not earning enough to pay the dividends on the preferred stock of the R. F. C. It is a loss to practically all of them, and they are eager to get rid of the preferred stock because of the burden on them.

Mr. WIGGINS. That is true.

Senator HUGHES. They try to get rid of it as fast as they can.

Mr. WIGGINS. More than half of it has been retired.

Senator WAGNER. It is as much as that?

Mr. WIGGINS. My recollection, Senator, is that the total advances are over \$1,000,000,000 and the total outstanding amount is less than \$500,000.

Senator TOWNSEND. Do you mean \$500,000 or \$500,000,000?

Mr. WIGGINS. I mean \$500,000,000.

Senator WAGNER. You have given us some interesting figures.

Mr. WIGGINS. I might say, in conclusion, in connection with the question the Senator asked, that in a long study of this whole field—and I am a small country banker and a small country businessman and have been managing director of a wholesale grocer business for 20-odd years, as well as president of a country bank, and I think I know first hand many of the problems of little business—my conclusion is that there is nowhere in the picture any lack of credit for business or for individuals that have any reasonable basis for credit that will give any reasonable assurance that the loans will be repaid, and that our difficulty today is largely in the field of working capital needs, and not the working capital needs that can be supplied properly by loans but the working capital field that must necessarily be supplied by share capital. That is where our deficiency is at the present time.

Senator HUGHES. Would you mind repeating that? I just did not get that.

Mr. WIGGINS. I made this observation; that, based on rather extensive experience in small business over a long period of time, my conclusion is that our financial difficulties today in small business in financing themselves is not so much in the field, or is not to any great extent in the field, that can be served by loans, but it is in the field that must be served by risk capital, or share capital, or ownership money. For instance, a bank can lend a business part of its working capital, but necessarily the owner of that business must have some working capital of his own in there as a cushion between the risk of the loan money and the possible losses of the business.

Now, no machinery, no new machinery, no machinery that I have been able to conceive of, can supply those funds except on the basis of taking an interest in the business, and if you will examine the loans made by the Federal Reserve banks under section 13b and the loans made by the R. F. C. for business and industry, you will find that the majority—a substantial majority—of those loans were made for the purpose of restoring working capital that has been lost, and that has been done by pledging the fixed assets of the business to provide working capital. It could be moved over in the working-capital side of the business, but secured by the fixed investments of the business,

and that is where the demand today is for funds. It is for working capital.

It is only in some cases that that working capital can be supplied through loans secured by fixed assets and put into working capital but in the vast majority of cases, where their fixed assets and other conditions are not satisfactory to assure the repayment of a loan, the money must be provided by ownership-investment.

Senator HUGHES. By going out and getting capital; by getting someone to come in and invest in your business.

Mr. WIGGINS. That is true.

Senator TOWNSEND. From your observations, is the demand for this character of funds very great?

Mr. WIGGINS. Senator, I can speak positively for my own community. I would be willing to pay anybody \$10 this morning who will find any man in my community who wants to borrow \$500 and has any reasonable security for it that will pass any reasonable bank's approval, and can't get it.

Now, as to the capital needs for working capital, for share money, for ownership money, for the risk money, there is a little demand here and there.

Senator TOWNSEND. But not great?

Mr. WIGGINS. But not great. In my own experience I know of only one case at the moment where a man needs \$10,000. He might need any amount, but he happens to need \$10,000 for a little business that has been broke, and he has taken it over and put in his own funds, two or three thousand dollars, and he wants to get somebody else to put in \$10,000 of ownership money, of share money, in order that he can conduct this little business. That is the only case of my own knowledge that I know of at the present time in my section.

Senator CLARK of Idaho. Of course, there is a demand to some extent, or is there, for 10-year money in smaller sums than underwriting concerns will touch; maybe 15-year money. A man wants to put a new front in his building, we will say, or wants to renew the set-up in the interior of his store and get new fixtures or maybe expand and take on additional space and put in new inventories. He cannot pay it back in 5 years—that is, he cannot comfortably and reasonably pay it back—but he can in 10 years or 15 years, and it is a sound, safe loan. As I say, it is too small for the underwriters. The testimony before this committee time and again has been that they won't touch anything less than \$10,000,000. There is not enough in it to put out a bond issue or security issue.

What do you think of that field in there? Do you not think that in that loan field there is really quite a demand? A bank normally won't take that type of loan. It is for too long a period, and it really ought to be in a bond issue of some kind.

Mr. WIGGINS. Senator, I think—and I have been analyzing this field, the demands and needs and sources—that there is at a point somewhere in the field you have mentioned what I call an hiatus—there is just a little vacancy there—and I think the R. F. C. has done a great job in filling that need in a great many cases. At the same time there are many small bond houses all over the country that are anxious and willing to handle these small issues.

I have had personal experience with one. We floated in the company in which I am interested, I think it was, \$400,000 of 5 percent

preferred stock, and my recollection is that it cost us about 4 points to sell it, which was very reasonable.

Senator TOWNSEND. What kind of business was it?

Mr. WIGGINS. It is a paper-manufacturing business.

Senator WAGNER. Were you able to sell them without difficulty?

Mr. WIGGINS. We did; yes, sir; with no difficulty at all. Of course, that particular business had \$3,000,000 worth of resources behind it, and it was one of the choice things to buy, but I do agree that there is a hiatus right in there to a limited extent. I do not think it is as great as people think, because banks have moved into that field to a considerable extent in recent years.

I know many cases of modernization of stores, and things of that sort, where they do not require 15 years, but they do require 5 or 6 or 8 years, and in some cases 10 years, and the banks have gone in and have been glad to get it. There are plenty of cases right here in Washington.

Senator WAGNER. Are there any other questions?

Senator ADAMS. Mr. Chairman, a year ago, at the time the matter was up before, I wrote to the Denver Clearing House, which represents all the larger banks there, and they have gone through their records and have submitted figures as to their acceptance or declination of loans. The banks have taken care of 1,175 loans, an aggregate of \$11,500,000, and during the same year 28 loans, aggregating \$275,000 were known to have been declined.

That was not a complete list of declinations, because the banks do not keep a record of all of them. Someone might come up to a counter and ask for a loan and they would tell him that it is an undesirable loan.

Senator WAGNER. What percentage was that?

Senator ADAMS. There were 1,175 loans accepted and 28 loans declined.

Senator MEAD. The figures given by the witness have been very impressive, as would be, naturally, any figures that pertain to the United States at large, whether they pertained to population or production or bank loans, or whatever the figures may be, but I recall that the witness admitted that the small loans were, for the most part, for 30, 60, 90 days, or a year at the most.

What the witness did not say, and what I would like to bring out, is this. There have been a great many loans made by the banks as a result of the direct or indirect influence of the R. F. C. I wonder if we could get a break-down of that volume of business in which the R. F. C. had a commitment or in which the banks were assured of a take-off or in which there was some participation—willing participation—either on the part of the R. F. C. or the Federal Reserve. It seems to me that there must be some activity where the R. F. C. or the Federal Reserve either participated or agreed to participate in some of this volume of business that the banks have done.

Senator TOWNSEND. Mr. Jones is here and he probably could tell us.

Senator MEAD. Mr. Jones, the witness gave us the very limited number of loans that the R. F. C. actually approved in a given period of time and the very meager amount of money as compared with the very large amount of money the private banks gave out, and it occurred to me, when those figures came out, that there was some of the R. F. C. money in some of this large volume of money that the banks

were crediting as their own loans. What I would like to do is to find out whether there is any direct or indirect R. F. C. help in that volume of business.

Senator TOWNSEND. You did not include R. F. C. money that had been loaned in conjunction with other banks?

Senator MEAD. There was no mention of R. F. C.

Senator TOWNSEND. I am asking him if he had any thoughts of that.

Mr. WIGGINS. I did not catch the question.

Senator TOWNSEND. The thought is that the R. F. C. has participated in loans that banks have made, as I get it from the Senator.

Senator MEAD. No. The witness said the banks make so many loans, and the witness said the R. F. C. made so many loans. What I would like to know is this: Is there any R. F. C. money that helped in the loans which the witness said the banks made?

Senator WAGNER. I think, Senator Mead, perhaps we can clear it up this way:

Mr. Wiggins, when you testified as to the number of loans made by banks—I think it went into a billion and some odd—

Mr. WIGGINS (interposing). The number of new loans made by the banks during 1939 was 12,675,000, in a total amount of \$23,115,000,000.

Senator WAGNER. Now, I wanted to ask you this: Are loans in which the R. F. C. participated with the banks included in that number or amount?

Mr. WIGGINS. I assume so. I assume that is the total amount of loans of the banks outstanding.

Senator MEAD. That is exactly what I wanted to know.

Senator WAGNER. You do not know how many or how much?

Mr. WIGGINS. I don't have any idea.

Senator MEAD. That brings out the fact that as a result of the activity of the Federal agency, the R. F. C., the volume of loans both in number and in the volume of money has increased immensely, and the R. F. C. should have some credit for that.

Senator ADAMS. As I recollect, the R. F. C. loans were one-hundred-thirty-odd million.

Senator MEAD. Yes.

Senator ADAMS. That would be in the \$23,000,000,000.

Senator MEAD. No.

Senator ADAMS. No; that would not be, either.

Senator MEAD. That is a separate and distinct R. F. C. enterprise, and it probably represents the loans that were turned down by the banks that finally, as a last resort, were obtained from the R. F. C., but it does not reflect the R. F. C. participation which is included in this large number of loans which the banks take credit for.

Senator WAGNER. Mr. Jones is here. Maybe he can clear it up.

Mr. JONES. I need about 10 minutes. What time are you going to adjourn?

Senator WAGNER. Suppose we take you now.

STATEMENT OF JESSE H. JONES, ADMINISTRATOR, FEDERAL LOAN AGENCY

Mr. JONES. I have this in letter form. I would like to read this:

In connection with your consideration of S. 3839, which deals with loans to business by the Federal Reserve banks and the Federal Treasury, beg to

advise that I favor credit to all deserving business and without too specific congressional restrictions.

While I doubt that any great amount of good will be accomplished through the passage of this law, I would favor its enactment amended as follows:

On page 3, by striking out all of the first sentence of section (c) after the words, "shall not exceed," on line 9, and insert the words: the amount of the paid-in capital stock of the banks, plus the accumulated surplus.

And I would strike out the rest to the end of the paragraph, on line 19, down to the word "Treasury."

Then I would strike out the last three lines on that page and all of pages 4 and 5.

Then I would add at the bottom as section (d):

Each Federal Reserve bank shall return to the Treasury any and all amounts heretofore paid to such bank by the Secretary of the Treasury under the provisions of this section representing a portion of the aggregate amount of \$139,299,557 originally paid by the Federal Reserve banks for stock in the Federal Deposit Insurance Corporation and thereupon said sum of \$139,299,257 shall be covered into the working balance of the Treasury.

The effect of that is that it authorizes the Federal Reserve banks to make business loans with their own money up to the amount of their capital and surplus.

Senator HUGHES. It takes away this commitment proposition?

Mr. JONES. It wipes that out and makes them return this balance to the Treasury.

We have all been trying to find out some way to help the Treasury, and they have that \$139,000,000 that they cannot use.

Senator HUGHES. Who is that?

Mr. JONES. The Treasury. They have got to hold that—

Senator HUGHES (interposing). Who is that? The Federal Reserve?

Mr. JONES. No; the Treasury.

Senator WAGNER. They have used \$26,000,000 of that, have they not?

Mr. JONES. They have used \$26,000,000 in 6 years. They were authorized to use \$280,000,000, but the \$139,000,000 is paid over from the Treasury.

Senator CLARK of Idaho. The member banks would not make the loans at all?

Mr. JONES. What do you mean by the "member banks"?

Senator CLARK of Idaho. The individual private banks. The Federal Reserve banks would make the loans directly?

Mr. JONES. In cooperation with their members.

Senator CLARK of Idaho. They would still be permitted to make commitments?

Mr. JONES. Yes. If the loan is too big to be made by the local bank let it go to the Federal Reserve. If the local bank is willing to take 25 percent, let it go to the Federal Reserve and get the other 75, or 50-50. The local banker goes to his own Federal Reserve bank where he is a member and proud of it.

Senator MEAD. In other words, you would set up in the Federal Reserve Board a sort of R. F. C. for the Federal Reserve System, limiting them to their own capital and surplus, is that it?

Mr. JONES. Yes; limit the amount they could lend to the capital and surplus.

Senator MEAD. The R. F. C. is a lending agency created by Congress. It has its limitations, and you would make similar limitations in the Federal Reserve System?

Mr. JONES. Mr. Eccles has testified that they have the facilities the equipment, and the men, and they have, just like we have. Let these member banks go and deal with their own Federal Reserve bank and work out the loan. Give them the authority to do it to a limited amount. They were authorized to lend up to \$280,000,000 in 1934.

Senator HUGHES. What puzzles me is that you want to have two agencies do practically the same thing; they are overlapping agencies.

Senator TOWNSEND. What authority do you give them here that they do not already have?

Senator HUGHES. It gives them money.

Senator TOWNSEND. No.

Mr. JONES. Senator, they say they can only lend up to 5 years—that is pretty long. They say they can only lend to established institutions—that is pretty broad itself, but they hide behind those two things as their alibi for not having made loans.

Senator TOWNSEND. What I am asking is: What authority do you give them under this bill that they do not have at the present time?

Mr. JONES. I have told you. If they want to make a 10-year loan, let them make it.

Senator TOWNSEND. All we are doing is increasing the time in which they could repay the loans made?

Mr. JONES. And, another thing, they could lend to a new institution. Under the present law, I think they can only lend to institutions existing at the time the act was passed.

They lend their own money instead of the Treasury's money. I believe that would be a helpful thing. If there was any competition, it would be with a member bank. Therefore, there is not going to be too much competition between them, but it would enable a bank, or a number of banks, through the Federal Reserve, to accommodate a borrower, and would divide the risk.

Senator HUGHES. The banks all have more money than they know what to do with.

Mr. JONES. Yes.

Senator HUGHES. How is the Federal Reserve going to help them except furnish them capital? They do not need that; they have all the money they need.

Mr. JONES. Banks come to us all the time and say, "We will take 25 percent of this loan if you will take 75 percent."

Instead of coming to us to get the 75 percent, let them go to the Federal Reserve banks. That is what I am thinking of. It may be 60 percent or 40 percent.

Senator WAGNER. Will their attitude be about the same as the R. F. C.'s in regard to these loans?

Mr. JONES. It has this advantage—and I will have something more to say later about the R. F. C.'s attitude—the banker is talking to his own Federal Reserve bank about a loan in his own community instead of talking to the R. F. C. about it, and I think it would produce better results. I think the Federal Reserve would make more loans if they were doing it themselves in cooperation with their own members.

Senator DANAHER. Why cannot they do it now?

Mr. JONES. They can do it now, except they have all this rigmarole, this shadow boxing. It has proved to be that because of the small amount of loans made, but if your bank wanted to make a loan to an industry in your community, bigger than it could afford to make, let it go to the Federal Reserve and ask that they take a part of it instead of coming to the R. F. C.

Senator CLARK of Idaho. Under the existing law, they have some restrictions as to adequate security that are different from the restrictions in your proposed law. What is that? Reasonable expectation of repayment, or something like that?

Mr. JONES. The Federal Reserve Act says "on a reasonable and sound basis"—what constitutes a sound loan depends on conditions and circumstances.

Senator CLARK of Idaho. Yes; but we did change that in the House, if you recall, 3 years ago.

Mr. JONES. You changed the authority of the R. F. C. Act to require such security as will reasonably assure repayment. The Federal Reserve Act has not been changed.

Senator CLARK of Idaho. We thought we were liberalizing it.

Mr. JONES. That is all you have when you have a Government bond.

Senator HUGHES. If it did not have that it would not be a sound loan.

Mr. JONES. I believe, gentlemen, it is worth your serious consideration. It would remove this hybrid thing we have now. It would release that \$139,000,000 and put back what is left into the general fund, and certainly the Treasury needs it.

Senator WAGNER. Mr. Jones, my attention was distracted when Senator Danaher asked you that question. I did not get the complete answer to that. They have available this sum of money now that is earmarked for their use to make industrial loans. Now we take that away from them. Why is that going to facilitate the loans?

Mr. JONES. Senator, here is the statement I made. If a banker in the Senator's community wanted to make a loan to an industry or a business for \$50,000 and that was more than the bank could afford to take, but it could afford to take \$15,000 or \$20,000 of it, instead of coming to the R. F. C. to get that money, let him go to the Federal Reserve bank and get it, but not out of this fund. Let the Federal Reserve make the loan together with its own member bank. Let it say, "We will take that risk." I think it is a service that the Federal Reserve ought to render.

Senator HUGHES. Let the Federal Reserve use their own money?

Mr. JONES. Yes; but limit it to the amount of their capital and surplus, so they cannot go broke doing it.

Senator WAGNER. Why will that accelerate the loans when you take away the funds from them that they can utilize now?

Mr. JONES. I believe, Senator, if you will put the responsibility on them maybe they will take advantage of it and maybe they will respond. They have not responded this way. They have done very little this way.

Senator WAGNER. Is that because of the definition of the kind of loan they may make? Is that the difficulty?

Mr. JONES. Take the restrictions out. Leave it to them as to what kind of loan they want to make. Let them make the loans. Let them be the judge.

Senator WAGNER. They have that power now except with respect to the fund of \$139,000,000. The restrictions are as to the use of the \$139,000,000 as working capital.

Senator DANAHER. That is not quite right. Right now they are limited to working capital loans.

Mr. JONES. Yes.

Senator WAGNER. Does that not refer only to the \$139,000,000?

Mr. JONES. Partially.

Senator WAGNER. That is what I am saying. Generally, outside of that, they can make loans?

Senator CLARK of Idaho. No; they cannot make any loans outside of that.

Mr. JONES. That is right; they cannot. With this suggestion of mine, they are the judges. If they want to make an industrial loan for 10 years, let them make it.

Senator DANAHER. What do you think of that, Mr. Wiggins?

Mr. WIGGINS. It sounds like common sense to me.

Mr. JONES. It wipes out all this nonsense that we have been dealing with.

Senator DANAHER. Putting it in another way, Mr. Jones, do you think that if the R. F. C. had not been in the picture, so that they could not load participation on to you, they would have gone further on their loans?

Mr. JONES. I do not know about that. Without intending to make any criticism of the Federal Reserve banks, the Federal Reserve banker is a graduated banker. A banker cannot graduate unless he is conservative, unless he has the last word on credits, and things like that. That is the general attitude. That is the attitude of the big banker. The small banker is all right in the country, but let him go to town and he graduates.

May I give you some figures now?

Senator WAGNER. Yes.

Mr. JONES. Congress passed this act in June 1934, 6 years ago, and the Federal Reserve banks were authorized to make loans direct to business to the extent of approximately \$280,000,000. To enable the Federal Reserve banks to make these loans, the Federal Treasury was authorized to advance to them an aggregate of \$139,299,557. This money was to be returned to the Treasury by the banks at the rate of 2 percent a year if earned—at best, in 50 years without interest. So they were, in fact, lending 50-cent dollars, and yet in lending 50-cent dollars the most they had outstanding at any one time was approximately \$32,000,000 in the 6-year period; \$27,500,000 of that they got from the Treasury. They keep that money; they do not give it back to the Treasury. They give the earnings from those loans back to the Treasury, up to 2 percent.

Therefore, the net result is that they have accumulated in their own surplus accounts \$26,500,000 of Treasury money, but it now belongs to the Federal Reserve banks, and they have only \$11,000,000 outstanding in loans.

The result of this Federal Reserve bank lending to business is that they have increased their surpluses and they have helped business very, very, little.

In comparison—and it is a tough job; I do not blame anybody, because a great many of the loans were hard to make; many of them are good—the R. F. C. has made something over 9,000 loans—they authorized that many—aggregating about \$550,000,000. Now, of that \$550,000,000 and those 9,000 loans, banks have agreed to take participation of 2,497 loans, aggregating \$67,793,895. We share in the loan and the security and repayments in proportion to our percentage of the loan with the bank.

Now, answering that other question, if the bank wants to carry the entire loan, we let him carry it. We charge a part of the interest for a take-out agreement for our participation in the loan. He can call on us any day he wants to for that money and get it.

Of that five-hundred-and-fifty-odd million dollars that we have authorized, one-hundred-and-thirty-four-odd million, for one reason or another, was canceled. The borrower did not take the money or he could not put up the security; \$129,000,000 is now still available to the borrowers and is being drawn on from time to time. Most of it is budgeted and is taken out as they need it and they pay interest on it only as they draw it.

We have disbursed, including participation with the banks, something like \$305,000,000 in the form of business loans; 37 percent of these loans in number have been for \$5,000 or less; 53 percent for \$10,000 or less; and 83 percent for \$50,000 or less. So that the great majority—the overwhelming majority—of these loans has been to the small-business man, and that is how we like it.

Senator WAGNER. What has been your experience in connection those loans?

Mr. JONES. I was going to give it to you now, because I think you ought to have that.

We have foreclosed 306 loans, aggregating \$18,535,801. Now, on those loans we will lose at least one-half. The security that we took, the plants, et cetera, will not liquidate more than half the loans, probably not quite half.

We have something over 900 loans aggregating approximately \$25,000,000, that are in default. A good many of those will have to be foreclosed.

We estimate that on all of our industrial loans the losses will average at least 10 percent. Banks just cannot make loans where they are going to have a 10-percent loss. We could not do it except that we make a little something on the other loans and that will take care of our losses, but we will lose something like 10 percent on those loans.

Senator WAGNER. I read in the New York Times, I think it was, that you sold \$20,000,000 worth of securities and made a million and a half in that transaction, so that there are other fields in which you make up for those losses?

Mr. JONES. Yes. We have accumulated \$285,000,000 or \$290,000,000 in surplus, as you have been told. I think \$100,000,000 to \$125,000,000 will cover our total losses. Business loans take two-thirds of all the time of the executives and the board. We try as hard as human beings can try to make them.

Senator WAGNER. Just looking at your enterprise as a business enterprise, would you regard it as a sound one?

Mr. JONES. Yes.

Senator HUGHES. Does it result in recognizing a class of borrowers who are good?

Mr. JONES. Yes; it does. In other words, our rates are 4, 4½, and 5 percent on industrial loans. We borrow money on 1 percent. We operate for about 1 percent. So that gives us a margin to accumulate these surpluses.

A well-run bank has got to do that, and we do favor the small business loan, because the sympathies of the country and the sympathies of Congress and the sympathies of all of us are with that fellow, and we try very hard to help him and we take pretty long chances. We have been given enough security always in appraised values, but a plant might be appraised at \$1,000,000 or \$100,000, and when you liquidate it you do not get much out of it.

Now, it is not all bad. We have had many loans that come right along and pay with the calendar. I could cite you any number of loans that have saved businesses and kept people employed and saved communities from W. P. A. rolls, and things of that kind.

I am heartily in favor of it, but it has its hazards and it has a big casualty percentage.

Is Senator Mead here?

Senator WAGNER. No; he just left.

Mr. JONES. I spoke to him about this, and the only suggestion he had about it was that he wondered how the Federal Reserve would feel about it. Naturally, they would want to be heard, I suppose, on this suggestion.

Senator WAGNER. You did not communicate with them in any way?

Mr. JONES. No; I just worked on it this morning, Senator. I found out you were going to have this and I have been trying to do something that would be helpful, and I think this would be helpful, particularly in an emergency.

Senator WAGNER (chairman of the subcommittee). Well, we will have to adjourn this hearing at this time. I will have to confer with Senator Mead as to the date on which we shall continue.

(Thereupon, at 12:15 o'clock p. m., an adjournment was taken, subject to the call of the chairman of the subcommittee.)

(The following letter was submitted by Mr. Eccles for inclusion in the record.)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Washington, June 24, 1940.

HON. ROBERT F. WAGNER,
Chairman, Banking and Currency Committee,
United States Senate, Washington, D. C.

DEAR SENATOR WAGNER: At the hearing on Senator Mead's bill, S. 3839, on Wednesday, June 13, 1940, you read extracts from a letter received from Mr. D. W. Bell, Acting Secretary of the Treasury, with respect to the bill and at the conclusion of the hearing you gave me a copy of Mr. Bell's letter for our information.

In reading Mr. Bell's letter I found a number of statements about which I should like to comment briefly for your records. Mr. Bell states that "It is the view of the Treasury Department that if the Federal Reserve banks are to continue to make industrial loans, as contemplated by the proposed legislation, they should be permitted to do so with their own funds and the Government should withdraw its funds heretofore advanced to the banks for this purpose and terminate the authorization for further advances."

For the reasons which I have stated in my testimony before your committee on S. 3839 and in correspondence with you, it is the position of the Board of Governors that section 13b of the Federal Reserve Act should be repealed and the Reserve banks entirely relieved of their responsibility for making this type of loan or that the section should be amended along the lines proposed in the bill.

It was the understanding of the Federal Reserve System, when section 13b was added to the Federal Reserve Act in 1934, that it was contemplated that the Secretary of the Treasury would pay to the Federal Reserve banks such amount up to \$139,299,556.99, the amount the Reserve banks subscribed to stock of the Federal Deposit Insurance Corporation, as was needed to enable them to make the advances and commitments authorized. The Secretary of the Treasury, however, issued regulations under which he advanced funds to the Federal Reserve banks amounting to approximately 50 percent of the outstanding loans and commitments of the Reserve banks. Following the issuance of the regulations by the Treasury Department, the Board conferred with the Department with respect to the accounting instructions to be issued to the Federal Reserve banks, and after several conferences instructions were prepared which the Board believed to be in accordance with the intent of Congress, and a copy was given to the Treasury. While these instructions have not received the specific approval of the Treasury, they have been the basis on which reports and payments have been made to the Treasury by the Federal Reserve banks.

Mr. Bell states in his letter that it is not clear from the language of the statute whether the 2 percent payments required to be made by the Reserve banks to the Treasury constitute payments of interest or payments upon the principal amounts advanced by the Treasury to the Federal Reserve banks. He also indicates that the enactment of S. 3839 "would still leave ambiguities whereby ultimate losses from these joint transactions could be charged to the funds advanced from the Treasury." Under the existing law the Federal Reserve banks are required to make the 2 percent payments in question only if they are earned, and they have done so with the understanding that the question as to whether the payments constitute a return of principal to the Treasury is being left for determination at a later date. No determination of this question has as yet been made, but it is eliminated that the enactment of S. 3839 would clear up both these questions and eliminate other ambiguities of the present law.

Mr. Bell points out that the aggregate outstanding loans and commitments of the Federal Reserve banks have, since April 1939, been less than the aggregate amount paid to the reserve banks by the Treasury, and that as loans and commitments were liquidated the Federal Reserve banks have withdrawn their funds and are treating the remaining loans and commitments outstanding as being financed entirely with funds received from the Treasury. This has been done because of a provision in the agreement between the Secretary of the Treasury and each Federal Reserve bank, required by the Secretary's regulations, that "Insofar as it is practicable to do so on a sound basis and in accordance with the provisions of Section 13b of the Federal Reserve Act and the regulations of the Federal Reserve Board thereunder, the Reserve Bank will keep all sums received from the Secretary under the provisions * * * of this agreement invested in loans, discounts, advances, or purchases made under section 13b of the Federal Reserve Act; * * *." Whether this procedure will result eventually in a profit or loss to the Treasury is impossible to state at this time, but on the basis of information now available it would appear that for the Federal Reserve banks as a whole the earnings on industrial advances and commitments will approximately offset the expenses and losses incurred in connection with such loans.

I understand that the letter from the Acting Secretary of the Treasury on this subject is to be included as a part of the record of the hearing which was held by your committee on June 13, 1940, and I will appreciate it if you will arrange to have a copy of this letter also included in the record of the proceedings on S. 3839.

Very truly yours,

MARRINER S. ECCLES,
Chairman.

X